Cochlear®
Hear now. And always

Cochlear Limited Annual Report 2020

Our story

Graeme Clark wanted to fix ears

From a young age, Professor Graeme Clark knew what he wanted to do: "I want to fix ears." He had watched his father, a pharmacist, struggle with hearing loss, and wanted to save others from the same hardship and isolation.

Then he spotted a shell

Professor Clark had a concept – and the ambition to see it through – but the challenges of the time made it difficult to turn idea into action. It was an encounter on a beach that was the final step Graeme needed. In a shell and a blade of grass – rigid at its roots but malleable at the tip – Graeme saw the structure that would allow an electrode array to adapt to any curve. It was here that the opportunity to connect hundreds of thousands of people to a life of hearing first came to light.

It helped to establish a company to bring that vision to life

Professor Clark changed the world – he and his team developed a new way of treating hearing loss. From the realisation of one man's dream, our global company was formed and hundreds of thousands of people have now experienced life's opportunities through hearing. Today we continue Professor Clark's dream and connect hearing implant recipients everywhere.

Our work is far from over

The history of our organisation has always been about transforming lives – giving people the opportunity to enjoy a life of hearing. Professor Clark was inspired to "fix ears" – and so too was Dr Anders Tjellström, who performed the world's first bone conduction hearing implant surgery in Gothenburg in 1977.

The work of these pioneering researchers – and their brave first recipients – laid the foundation for our company. This drive has always been a part of our DNA – we gain our inspiration from the people we serve and support. That's what inspires our journey forward.

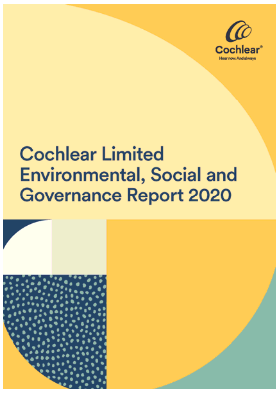
Contents

Shareholder reports

Cochlear publishes a number of online shareholder reports aimed at improving transparency and making information easier to access. They are a great companion to the Annual Report and are all available at the Investor section of the website, www.cochlear.com.

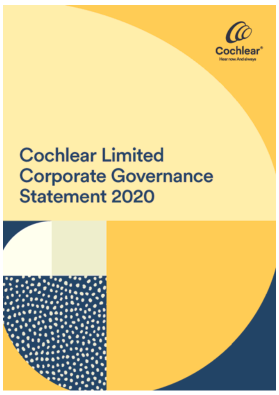
Strategy Overview

The Strategy Overview provides an insight into Cochlear's strategy to retain market leadership, grow the hearing implant market and deliver consistent revenue and earnings growth over the long term.



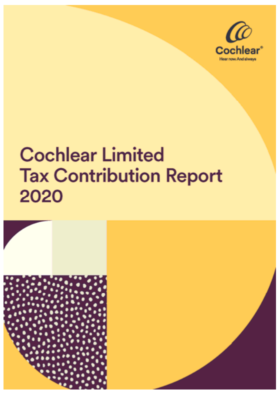
ESG Report

The ESG (Environmental, Social and Governance) Report outlines how we aim to improve the impact we have on our communities, the environment and our employees and reflects our commitment to high standards of corporate governance.



Corporate Governance Statement

The Corporate Governance Statement summarises the Company's corporate governance practices and incorporates the disclosures required by the ASX Corporate Governance Council's Corporate Governance Principles and Recommendations (3rd Edition).



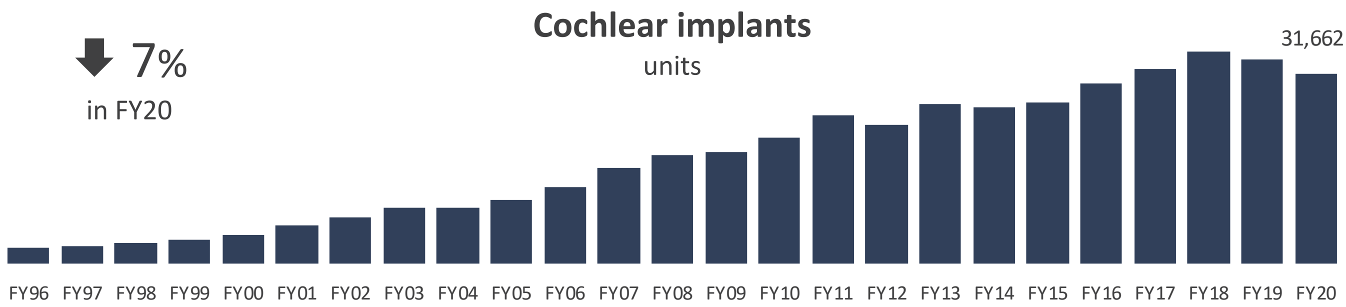
Tax Contribution Report

The Tax Contribution Report covers Cochlear's taxes paid in Australia and globally and details the global tax strategy.

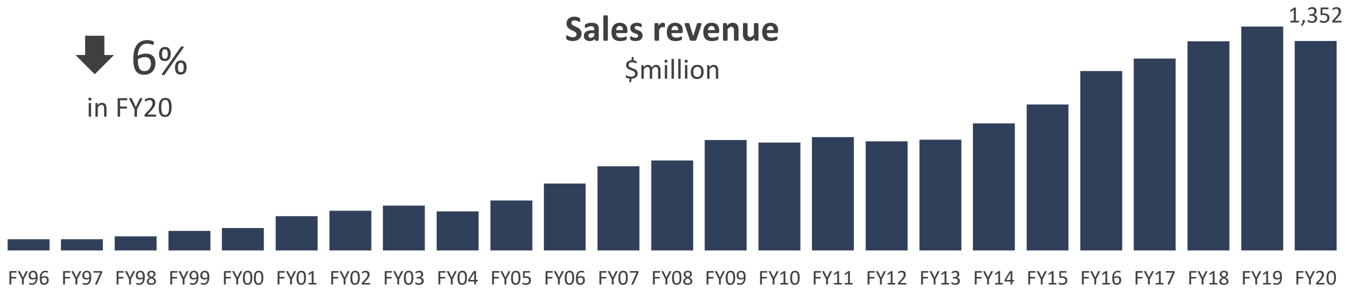
Financial history

Cochlear has a long track record of delivering growing sales revenue, profits* and dividends, disrupted in FY20 by the impact of COVID-19.

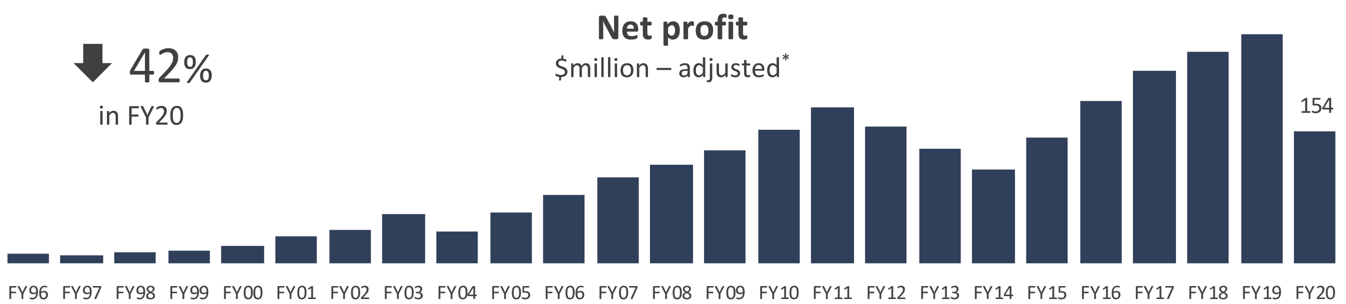
7%
in FY20



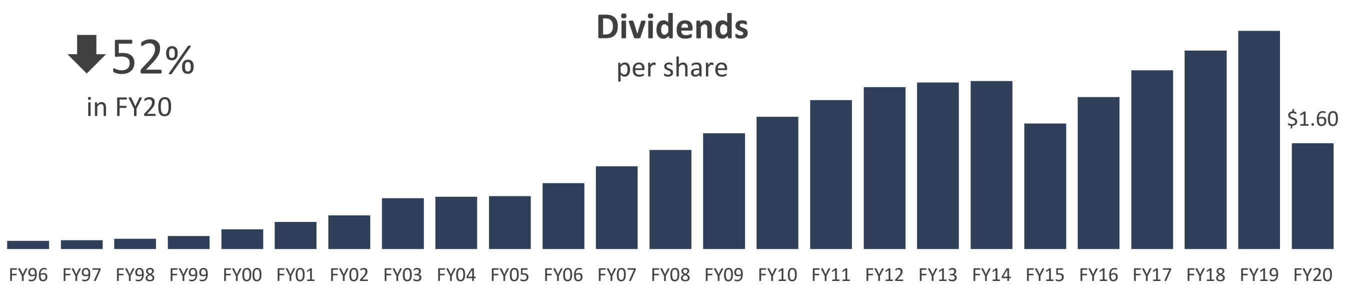
6%
in FY20



42%
in FY20



52%
in FY20



* Excludes the following items after tax: FY12 - product recall costs of $101 million, FY14 - patent dispute provision of $16 million, FY19 - $11 million innovation fund gains and FY20 - $416 million patent litigation expense and $24 million innovation fund gains.

Letter to shareholders

Cochlear had a strong start to FY20 with cochlear implants delivering a 13% increase in unit growth in the first half. The launch of the Cochlear™ Nucleus® Profile™ Plus Series cochlear implant was well-received, driving share gains in many markets. The impact of COVID-19 on the business during the second half was substantial, with the deferral of cochlear implant surgeries across the world. As COVID-19 started to impact the business, we were very clear that we wanted to emerge from the pandemic in a stronger competitive position, placing a high priority on keeping our valuable workforce intact and continuing to invest in our R&D programs and market growth activities. While still early days, surgeries have resumed in many markets.

The impact of COVID-19 on profitability was significant with underlying net profit declining by 42% to $153.8 million. After factoring in patent litigation expenses and innovation fund gains, Cochlear recorded a net loss of $238.3 million for FY20. In response, we have taken actions to strengthen our balance sheet and liquidity position to enable the business to weather the expected business disruption caused by COVID-19.

Throughout this time, Cochlear has been focused on keeping all employees safe, and supporting customers and communities, while following all local and country guidance in the regions we operate throughout the world. The team at Cochlear shares its heartfelt empathy with the communities impacted worldwide by COVID-19. As the world responds to this pandemic, we remain committed to supporting our customers, employees and communities to ensure that the vital work of delivering implantable hearing solutions to patients continues.

Cochlear implants

The cochlear implant business delivered strong growth in the first half of the year as the Nucleus Profile Plus Series cochlear implant was successfully launched across major markets. The positive momentum was however disrupted in the second half by COVID-19 with elective surgeries deferred across the world as infection rates grew. We experienced a significant and rapid decline in revenue from mid-March to early-May, the point at which surgeries began to resume.

By the end of June, market conditions still varied greatly across our markets with surgery volumes recovering quickly in China, the US, Germany, Benelux and Australia and more slowly in the UK, Spain and Italy. Surgeries across most emerging markets, including India and Latin America, have remained very low as COVID-19 cases continue to grow.

The portfolio was boosted by the addition of a number of new products including the Cochlear™ Nucleus® Profile Plus with Slim 20 Electrode and the Cochlear™ Nucleus® Kanso® 2 Sound Processor which are currently being launched across major markets.

Services

Services were materially impacted by COVID-19 in the fourth quarter of FY20. While some recipients have been able to access sound processor upgrades remotely, clinic closures have delayed access to sound processor upgrades for many people.

Cochlear's remote servicing capability, with tools including Cochlear™ Link and Remote Check, are assisting clinicians and recipients with performance, mapping, and troubleshooting in markets where they are approved. Many countries and clinics have been adapting, enabling greater levels of remote access and programming to assist recipients unable to visit clinics as a result of COVID-19. In recognition of the importance of providing support, the FDA fast-tracked approval of Remote Check in April.

Acoustics

In the first half, we experienced some loss of market share from competitor product launches. The market also slowed more than expected in anticipation of the launch of the next generation bone conduction implant, the Cochlear™ Osia® 2 System, which commenced its rollout in the US in February. Like cochlear implants, the second half was materially impacted by COVID-19 due to the delay of elective surgeries.

Acoustics revenue is largely generated from the US and the UK. Surgery volumes have improved in the US since May with increasing demand for the Osia 2 System. Acoustic implant surgeries in the UK, however, have not yet restarted following the COVID-19 shutdowns.

Managing through the pandemic

Since the outbreak of COVID-19, the normal structures of business life needed to rapidly and radically adapt. We changed the way we managed the business, setting aside the normal planning cycles, and enacting our business continuity plan. Guided by our mission, our immediate priorities were to:

- Ensure the health and safety of our employees;
- Provide ongoing support to our recipients, clinics and professional partners; and
- Maintain the financial health of the Company.

Our employees represent around two-thirds of our operating costs. They have valuable experience and make great contributions to Cochlear's mission. We do not want to reduce our workforce as we believe the disruption will be temporary. We have however significantly reduced non-essential spending and capital expenditure and will continue to do so until there is a sustained increase in surgeries. We also implemented a hiring freeze, with temporary pay reductions for the Board and senior management across the business in the last quarter of FY20.

We changed the way we worked together with the majority of employees working from home across the globe from mid-March. The rapid and successful transition to communicating via video meetings, best practice sharing sessions, rebalancing workloads across the business via our 'marketplace' initiative and conducting weekly global town hall meetings has actually enhanced workplace engagement for most, with many of the new ways of doing business to continue post pandemic.

Cochlear's teams have remained focused on providing support to recipients, while continuing their outreach programs with candidates through the Company's direct-to-consumer marketing efforts. The rapid adoption of online and video conferencing tools with our professional partners, candidates and recipients is to be commended and has ensured that we can continue to provide valuable education and support throughout the pandemic.

Keeping people connected and informed via regular employee video briefings

We have continued to invest in the R&D pipeline with the majority of projects progressing to schedule, including products currently in the regulatory approval process. With the rapid changes in the operating landscape, including clinic closures and access to telemedicine in some markets, we took the opportunity to review our R&D priorities, opting to scale up our connected care efforts even more.

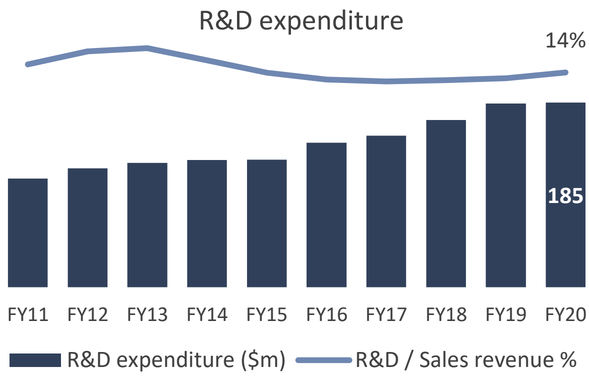
We have spent many years developing our remote care solutions, with the connectivity of the Cochlear™ Nucleus® 7 Sound Processor to the cloud enabling a suite of remote capability. We are now starting to gain regulatory approval for remote care solutions that can provide recipients and audiologists with the ability to access efficient and convenient care. We continue to work on securing reimbursement for these solutions as a way to drive greater adoption.

Customer servicing has been largely unaffected with the Global Repair Centre fully operational. Cochlear's manufacturing and service and repair centres have been deemed as essential services and continue to operate. Manufacturing output of cochlear and acoustic implant systems has been reduced to manage inventory levels.

The supply chain continues to be largely intact. Our conservative approach to inventory management and long-term supplier relations ensured that there were no supply shortages for components. The business continues to carry adequate levels of inventory for most components and is managing distribution in line with customer demand to enable continued supply of products to customers.

Maintaining the financial health of Cochlear ultimately enables us to pursue our mission. The liquidity position has been strengthened through a $1.1 billion capital raising and $225 million increase in debt facilities during March and April.

Cochlear webinars providing online education and support for professionals and recipients



Continuing to progress the R&D pipeline

There is no doubt the last few months have been very challenging. As we progressively return to working from the office, we are also taking the opportunity to learn. Many of the new ways of doing business both internally and with our customers will be continued post pandemic.

Retaining market leadership

Cochlear has been the global leader in implantable hearing solutions for 40 years. The investment in R&D aims to strengthen our leadership position through the development of market-leading technology.

In FY20, we invested $185 million in R&D, in line with FY19 levels, and representing 14% of sales revenue. Investment in the R&D pipeline continued despite COVID-19 with the majority of projects progressing to schedule, including products currently in the regulatory approval process.

The highlight for the year has been the approval of a number of important new products spanning all components of the product portfolio, with many approvals received either just before, or during, the COVID-19 shutdowns. These include:

Cochlear™ Nucleus® Kanso® 2 Sound Processor

Implants and electrodes

- Cochlear™ Osia® 2 System
- Cochlear™ Nucleus® Profile™ Plus with Slim 20 Electrode

Sound processors

- Cochlear™ Nucleus® Kanso® 2 Sound Processor
- Cochlear™ Nucleus® 7 Sound Processor for Nucleus 22 implant recipients

Clinical and surgical support tools

- Custom Sound® Pro fitting software
- Nucleus® SmartNav System

Connected care

- Remote Check solution for cochlear implants

Cochlear™ Osia® 2 System

Nucleus® SmartNav System

Growing the market for hearing implants

As the global leader, Cochlear is focused on driving long-term market growth by transforming the way people understand and treat moderately severe to profound hearing loss through awareness and access activities. In FY20, we continued to invest in expanding our programs for driving growth of the adults and seniors segment which include direct-to-consumer marketing activities, building hearing aid channel referrals from the hearing aid and ENT channels, and standard of care initiatives aimed at building a consistent treatment pathway for adults with severe to profound hearing loss.

The Cochlear Provider Network continued to expand and is building education of the indications and benefits of cochlear implants to hearing aid audiologists in the US and is starting to provide a referral pathway to cochlear implant surgeons.

We also hit some key milestones with improved indications and/or funding for our products across a number of markets including:

Expanded indications

- US: approval to lower the age of paediatric cochlear implantation from 12 to nine months for Cochlear's implant portfolio
- Belgium: expansion of reimbursement criteria for cochlear implants to include candidates with a severe hearing loss
- Czech Republic: funding for cochlear implants for adults
- France: reimbursement approved for Baha sound processors

FDA approval lowers the age of paediatric cochlear implantation to nine months

In March, Cochlear™ Nucleus® implants obtained FDA approval to be implanted in children from nine months of age, down from 12 months, for children with bilateral, profound sensorineural hearing loss.

Cochlear's Nucleus implants have been FDA approved for use in children since 1990, with the last indication change for lowering the age of implantation for children, achieved in 2000. Decades of research and current surgical and clinical practice underscore the efficacy of earlier implantation for children so that they can achieve their personal best language and speech outcomes.

The research and support in practice by trained hearing health professionals provided the foundation to approve the lowering of the indication to nine months, along with the considerable developments in technology and evolving speech coding strategies in modern day cochlear implant devices.

Our market access teams endeavour to expand the availability and/or funding of our products to those who can most benefit. This approval ensures children born deaf can have access to sound via cochlear implantation sooner and provide them with earlier opportunities to develop speech and language which can help them meet developmental milestones with their peers born with hearing.

Early intervention is important for developing language and social skills

Cost-effectiveness of cochlear implants in adults

As we look to the future, we believe the cost-effectiveness of health interventions will become a more important consideration in the allocation of healthcare spending.

Payers are increasingly demanding cost-effectiveness data to support funding for health interventions. We believe Cochlear is well positioned with numerous studies demonstrating the cost-effectiveness of cochlear implants for both children and adults.

For a pre-lingual deaf child, the return to society is more than 13 times every dollar spent on a cochlear implant solution based on the cost savings in education and improved productivity as an adult.

Dementia and other cognitive decline diseases are some of the costliest conditions to treat in the world, at an estimated US$1 trillion in 2018 and estimated to double by 2030. Unfortunately, individuals with severe hearing loss are almost five times more likely to develop dementia than people without hearing loss. The effective use of hearing aids and implants is cost-effective and has been proven in adults and seniors with an estimated return on investment of 10:1.

Studies demonstrate the cost-effectiveness of cochlear implants for adults

China manufacturing facility and new US head office

In 2017, after more than 20 years operating in China, Cochlear announced plans to establish a A$90 million manufacturing facility in Chengdu, Sichuan Province. This China Expansion Project is part of our supply chain strategy, to ensure we expand our global manufacturing capacity to facilitate local market growth and provide additional manufacturing support for products in China and emerging markets.

Major construction milestones were completed by the end of June, with finalisation of interiors and commissioning expected by the end of 2020. The regulatory approval process is expected to take around two years, with manufacturing to commence once we have received the necessary regulatory approvals.

In May, our US team celebrated the opening of our new US headquarters located in Denver, Colorado. The new US$20 million headquarters has been designed to meet the growth needs of the business over the coming years. The new, larger office includes training rooms, a customer experience centre, a fitness centre and café.

Construction of Cochlear's China manufacturing facility to be completed by the end of 2020

Cochlear's new US head office in Denver, Colorado opened in May

Adverse litigation outcome

In March, the US Court of Appeals for the Federal Circuit in Washington, DC affirmed the US District Court award of patent infringement damages against Cochlear and its US subsidiary Cochlear Americas in the lawsuit by the Alfred E Mann Foundation for Scientific Research (AMF) and Advanced Bionics LLC (AB), with payment of US$280 million, including post judgment interest, made in June. Cochlear intends to lodge an appeal with the US Supreme Court against the Judgment.

The case related to two patents that have long expired. The Court had previously invalidated the first patent with the remaining patent much narrower in scope. We believe the amount of damages awarded was out of proportion with the limited application of the patented feature, acknowledging that inflated damages awards are a risk of patent disputes in the US.

Subsequent to year-end, Cochlear agreed to a settlement with AMF and AB of pre-judgment interest and attorneys' fees totalling US$75 million. At 30 June 2020, Cochlear has provided US$75 million in relation to this settlement which is included in the patent litigation expense within the Income Statement. The settlement is conditional upon the outcome of an appeal by Cochlear to the US Supreme Court against the US$280 million Judgment. If Cochlear's Supreme Court appeal is successful, there may be a new trial to redetermine the quantum of damages.

As the patent at issue in the litigation has expired, the judgment will not disrupt Cochlear's business or customers in the US.

Board renewal

Over recent years we have implemented a Board renewal process, bringing onto the Board a number of new directors with diverse backgrounds and relevant experience. We have sought to maintain a balance of continuity, and to introduce new skill sets. We have been pleased with all the recent appointments, with the new directors adding great perspective and value to our Board discussions.

Two new directors join the Board this year, Michael Daniell and Christine McLoughlin. Michael was appointed in January and has worked in the medical device industry for over 40 years. He has extensive executive leadership experience and was Managing Director and CEO of Fisher & Paykel Healthcare Corporation Ltd from November 2001 to March 2016.

Christine will join in November and is a highly respected company director with domestic and international experience in financial and health services and telecommunications. She is recognised for her achievements in driving continuous improvements in organisational culture and performance, and her focus on creating value for shareholders by delivering for customers.

Long-serving non-executive director Donal O'Dwyer will be retiring from the Company's board at the end of the 2020 annual general meeting. Donal has provided invaluable counsel in his 15 years of service to the Cochlear board. His extensive technical expertise in the medical device and healthcare industries, along with his significant management experience globally in these industries, have contributed greatly to Cochlear's strategic direction. On behalf of the board, I would like to sincerely thank Donal for his service and contribution to Cochlear and wish him well for the future.

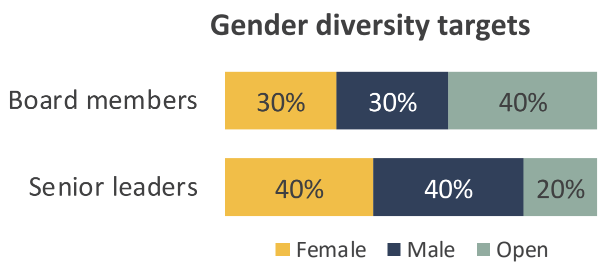
Establishment of gender diversity targets

Our Diversity and Inclusion Framework, launched just over two years ago, is driving greater awareness across the organisation of the importance of a diverse and inclusive workplace.

Achieving gender equality is one important element of our Diversity and Inclusion strategy. We strive for gender balance of 40:40:20, which means that 40-60 per cent of either gender is represented (40% women, 40% men, 20% open). While over 50% of Cochlear's employees are female, the representation of females reduces as the level of seniority increases.

In this context, we have set a target to achieve at least 40% female representation amongst our senior leaders within three years, from 36% today. At Board level, we are targeting 30% female representation over the next two years, from 20% today.

Achievement of this target is being supported by focused activities in the areas of Talent Succession and Talent Acquisition, with the aim of increasing our pipeline of female talent. A range of additional activities and policies recognised as key enablers to gender equality continue to be implemented to support improved access to work for all employees. These include a focus on continuing to embed flexible working for employees globally, further deployment of our Inclusive Leadership programs with a focus on unconscious bias education for all leaders, and continuing work to ensure gender pay equity across our global workforce.



Trading update and FY21 outlook

As COVID-19 started to impact the business, we were very clear that we wanted to emerge from the pandemic in a stronger competitive position, placing a high priority on keeping our valuable workforce intact and continuing to invest in our R&D programs and market growth activities. Our market position has strengthened during FY20, with growing share and a continuing shift to our cochlear implants with perimodiolar electrodes, now representing around 60% of our implant mix in markets where it is available. And the product portfolio has been expanded with a range of new products that are expected to drive further improvements in share.

In April cochlear implant revenue fell by nearly 60%. We have been experiencing an improving trend in trading since May with the recommencement of surgeries across most markets. In June/July cochlear implant revenue was 85% of last year as a result of a combination of new surgeries and rescheduled surgeries. There continues to be a significant level of variability across countries, with developed market momentum well ahead of the emerging markets.

For the developed markets, unit volumes were in line with last year for the June/July trading period, reflecting both a return to surgery and market share gains. While the resumption of surgeries in the US, Germany, Japan and northern Europe has been quite rapid, there are still a number of markets with lower levels of surgery activity including the UK, Italy and Spain.

It has also been pleasing to see that the segment mix, that is, the split between children, adults and seniors, reflects the pre-COVID-19 mix across most countries. In countries where surgery rates remain relatively low, the clear priority continues to be the implantation of children.

While the resumption of elective surgeries is positive, we caution that there is still risk, noting that second waves of COVID-19 cases are likely to remain a reality for some time and may result in new restrictions to elective surgery, complicating recovery plans and timing.

We also recognise that the surgeries currently occurring, particularly for adults and seniors, include a catch up of delayed surgeries from March to May. We will get a clearer picture of the impact of clinic closures in April and May on the new candidate pipeline over the next few months. While the majority of clinics have re-opened, many are still running below capacity as they recommence operations sensibly, mindful of the need to continue social distancing disciplines. As a result, we expect there to be some impact on the number of patient assessments for cochlear and acoustic implants until clinic throughput normalises. Our direct-to-consumer activities, which continued throughout COVID-19 shutdowns, have been aimed at providing additional support to candidates, and potential candidates, and it is hoped that these activities may assist in more quickly rebuilding the candidate pipeline.

For the emerging markets, unit volumes were at 50% of last year for the June/July trading period. Surgeries in China are growing quickly, and we remain committed to continuing to invest in further growth. In other markets, including India and Latin America, surgeries have remained very low as COVID-19 cases continue to grow.

Services revenue run rates have been improving since May with June/July revenue at around 70% of last year. The launch of the Kanso 2 Sound Processor, the growing recipient base and the adoption of remote care tools are expected to underpin demand for upgrades over the longer term. In the near term, however, we expect clinic capacity for upgrades to be lower than normal.

Acoustic revenue run rates have also been improving since May with June/July revenue at around 70% of last year. Surgery volumes have been recovering in the US since May with strong demand for the Osia 2 System. Acoustic implant surgeries in the UK, however, have not yet restarted following the COVID-19 shutdowns. We continue to be excited about the potential for the Osia 2 System. It represents a significant improvement in performance, aesthetics and quality of life for bone conduction patients and has received an enthusiastic response from surgeons and patients in the US since launch. We are aiming to get regulatory approval for the Osia 2 System in Europe by mid 2021.

Cochlear’s liquidity position is strong following the $1.1 billion capital raising and expansion of debt facilities in March. Combined net cash and undrawn debt facilities total $987 million as at 30 June. With revenues improving, operating cash flow is currently around breakeven levels. In considering use of cash for FY21, we are forecasting around $90 million in capital expenditure. It should also be noted that the payment of US$75 million in prejudgment interest and attorneys’ fees relating to the litigation case is conditional upon the outcome of an appeal by Cochlear to the US Supreme Court. Cochlear will deposit the funds into an escrow account pending the outcome of the appeal.

In March, Cochlear announced the suspension of the dividend until trading conditions improve. The Board expects to resume payment of a dividend once a clear and sustained improvement in sales revenue has been established and cash flow generation is sufficient to support its resumption.

Due to the uncertain timing of a global recovery from the pandemic, we cannot reliably estimate FY21 revenues, so will not be providing earnings guidance. A trading update will be provided at the annual general meeting on 20 October. Our investment priorities for FY21 will be focused on market growth activities and strengthening our competitive position, while continuing to limit non-essential spending until we have greater confidence in the outlook. There are a number of cost base considerations for FY21, which may be adapted if trading conditions materially change:

- Operating expenses (excluding R&D) are forecast to increase by around 4% with the growing investment in market growth activities and re-instatement of the short-term incentive provision, partly offset by lower levels of more discretionary spending;
- Investment in R&D is expected to increase to around $190-195 million;
- We expect to receive some further government support following the receipt in FY20 of $24 million in COVID-19-related government assistance from a number of countries;
- FX contracts gains/(losses) are expected to be close to zero as a result of minimal hedging in FY21; and
- Depreciation and amortisation (including AASB16-related) is expected to be around $80 million.

Longer-term outlook

As we look to the future, we remain confident about the opportunity to grow our markets. There remains a significant, unmet and addressable clinical need for cochlear and acoustic implants that is expected to continue to underpin the long-term sustainable growth of the business.

As we transition from dealing with a health crisis to assessing the long-term economic impacts of the pandemic, we are thinking more about what may change in the hearing implant landscape. There will no doubt be opportunities as well as risks that mean we may need to adapt our strategy.

Front of mind is the debt burden that economies will face and the increased competition for health funding. We see a real potential for payers to accelerate the adoption of health economic considerations, allocating spending to more cost-effective interventions. Cochlear implants provide a cost-effective solution for all age groups, delivering significant returns on the investment made by the healthcare system. While we believe our intervention is well-positioned, it is too early to understand what, if any, implications there will be for healthcare spending or how our products may be prioritised.

The pandemic has also driven the rapid adoption of telehealth and telemedicine which may lead to faster than expected structural changes in healthcare delivery. We experienced this first hand with the FDA fast-tracking the approval of our Remote Check solution in the US. Our professional partners too have shown greater interest and demand for our connected care solutions over the last few months which also include Cochlear Link and Remote Programming in many markets. We have been investing in connected care solutions for many years and believe they provide the opportunity to open up access to our products and optimise outcomes for recipients by transforming the care model while delivering efficiencies to clinics.

We are also aware that there may be other risks and we are carefully monitoring business performance.

Our employees

Cochlear has a diverse global workforce focused on our business and on transforming the lives of people with hearing loss. We employ over 4,000 people and sell our products in over 180 countries. The knowledge, expertise and passion of our employees are key to our future and the focus on delivering excellence for our customers is an important part of our success and our market leadership position.

Our employees understand the importance of Cochlear being successful over the long term so that we can continue to support our recipients. There are few companies that start a lifetime journey with each new customer every day.

On behalf of the Board, we congratulate and thank all Cochlear employees for their outstanding efforts and contributions this year.

Rick Holliday-Smith
Chairman

Dig Howitt
CEO & President

Market leadership

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New product approvals

The highlight for the year has been the approval of a number of important new products spanning all components of the product portfolio, with many approvals received either just before, or during, the COVID-19 shutdowns. These include:

Implants and electrodes

Cochlear™ Osia® 2 System

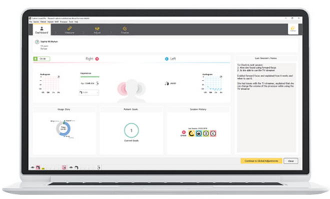
Cochlear™ Nucleus® Profile™ Plus with Slim 20 Electrode

Sound processors

Cochlear™ Nucleus® 7 Sound Processor for Nucleus® 22 implant recipients

Cochlear™ Nucleus® Kanso® 2 Sound Processor

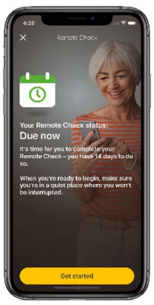
Clinical and surgical tools



Custom Sound® Pro fitting software

Nucleus® SmartNav System

Connected care



Remote Check solution for cochlear implants

Cochlear™ Osia® 2 System

The Cochlear™ Osia® 2 System expands the Acoustics portfolio into the next generation of bone conduction hearing solutions. It is the world's first active osseointegrated steady-state implant, using digital piezoelectric stimulation to bypass damaged areas of the natural hearing system, sending sound vibrations directly to the cochlea. Pre-market trials have demonstrated significant improvements in outcomes for patients[1] over traditional bone conduction hearing solutions, and we are already experiencing high demand for the new implant in the US.

We believe the Osia 2 System is the right product to drive category growth and deepen penetration of bone conduction implants over time. The new implant provides a significant improvement in performance and aesthetics for bone conduction patients with an enthusiastic response from surgeons and patients over the past few months.

The Cochlear™ Osia® 2 System provides a significant improvement in performance and aesthetics for bone conduction patients

Cochlear™ Nucleus® Profile™ Plus with Slim 20 Electrode

In February, Cochlear received FDA approval for the Cochlear™ Nucleus® Profile™ Plus with Slim 20 Electrode (CI624). The Slim 20 Electrode expands Cochlear's portfolio which consists of the slimmest atraumatic electrodes on the market, providing an option for surgeons who prefer an insertion depth of up to 20mm with a lateral wall electrode.

The addition of the Slim 20 Electrode further strengthens Cochlear's market-leading portfolio of electrodes designed for structural preservation, hearing performance, and surgeon preference.

Cochlear™ Nucleus® Profile™ Plus with Slim 20 Electrode (CI624)

Cochlear™ Nucleus® Kanso® 2 Sound Processor

In July, we received FDA approval for the Cochlear™ Nucleus® Kanso® 2 Sound Processor, the world's smallest[2] off-the-ear cochlear implant with proven hearing performance technologies[3-6]. It is the first and only off-the-ear cochlear implant sound processor to offer direct streaming from compatible Apple or Android™ devices, and is compatible with the Nucleus Smart App, enabling control of device settings, functions and information.

The Kanso 2 Sound Processor features an integrated rechargeable battery[7] and the highest possible water resistance rating for any off-the-ear cochlear implant sound processor, giving users the freedom to live an active lifestyle.

To help users hear more of what they want to listen to, the Nucleus Kanso 2 Sound Processor features proven hearing performance technologies. Dual microphones filter out background noise to help provide better hearing performance in noise compared to a single microphone[4]. With ForwardFocus, users can reduce noise from behind them to help them focus on conversations in front of them[6]. SmartSound® IQ with SCAN helps users to hear more clearly in a range of listening environments by capturing sound through dual microphones and analysing surroundings before automatically adjusting the settings for the hearing conditions[3-5].

The Kanso 2 Sound Processor features a simple, durable all-in-one design that makes it easy to use. Unique button-free control with an automatic on/off function helps to simplify the experience. The device is a practical choice for children as it is simple for parents to check microphone functionality, monitor their child's hearing performance or locate a missing processor using the Nucleus Smart App.

The Cochlear™ Nucleus® Kanso® 2 Sound Processor is the world's smallest off-the-ear cochlear implant sound processor, and the first to offer direct streaming from compatible Apple or Android™ devices

Cochlear™ Nucleus® 7 Sound Processor for Nucleus® 22 implant recipients

The Cochlear™ Nucleus® 7 Sound Processor is now compatible for cochlear implant recipients with a Nucleus 22 implant. This means that Nucleus 22 implant recipients can now upgrade to Cochlear's latest behind-the-ear sound processor and, for the first time, access direct smartphone connectivity and streaming.

The Nucleus 7 Sound Processor is the world's first and only behind-the-ear cochlear implant sound processor to offer direct streaming, connectivity and control from a compatible Apple or Android™ device. It is also the smallest and lightest[6] behind-the-ear cochlear implant sound processor, designed for comfort and to help improve hearing performance[3,8].

The Nucleus 22 implant was Cochlear's first commercial implant, first released in 1982. There are more than 17,000 people around the world with a Nucleus 22 implant. This upgrade means that for the first time people who have benefited from their implant for almost 40 years can access direct smartphone connectivity in a smaller and lighter design.

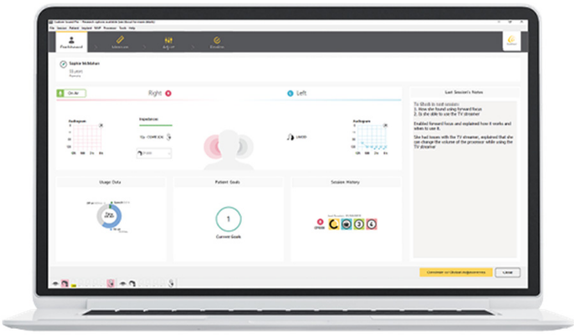
Enabling people who have benefited from their implant for almost 40 years to access direct smartphone connectivity

Custom Sound® Pro fitting software

Custom Sound® Pro supports clinicians in fitting Cochlear implant sound processors. The software harnesses almost 40 years of experience and input from thousands of clinicians worldwide[9].

The Custom Sound Pro fitting software keeps the patient at the centre of care with a new patient dashboard and Patient Goals feature, promoting patient engagement and facilitating more effective tracking of progress between appointments[10]. With an intuitive layout, an integrated workflow for bilateral fittings and increased on-air time, the software is designed to enhance the fitting experience for clinicians and their patients.

To help patients experience the best possible hearing performance, it is important that programming software for cochlear implant sound processors provide flexibility and be easy to use. The new Custom Sound Pro fitting software was created by clinicians, for clinicians, enabling hearing health professionals to deliver tailored care for every patient.



Custom Sound® Pro fitting software

Nucleus® SmartNav System

The Nucleus® SmartNav System is a new tool to support surgeons in optimising electrode placement during cochlear implant surgery.

The Nucleus SmartNav System delivers wireless, actionable intraoperative insights to support electrode insertion with real-time navigation, providing surgeons with added assurance of a successful surgical outcome for their patients.

The system consists of an innovative iPad-based solution and a surgical sound processor that presents an intuitive workflow to support surgery, giving surgeons additional feedback for in-theatre decision making.

Nucleus® SmartNav System

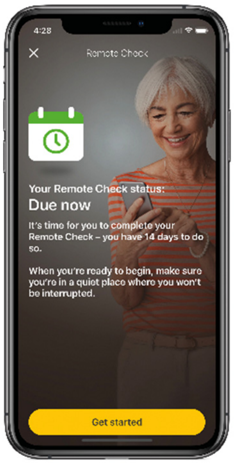
Remote Check solution for cochlear implants

In April, Cochlear obtained FDA approval for its Remote Check solution. Remote Check is the first telehealth patient assessment tool for cochlear implant recipients. It is designed to be a convenient, at-home testing tool that allows people with a Nucleus 7 Sound Processor to complete a series of hearing checks from their compatible iOS device using the Nucleus Smart App. Results are then sent remotely to the recipient's clinic for review by their clinician.

Remote Check was developed to conduct routine cochlear implant checks outside the hearing clinic. The technology has been tested in previous pilots in five countries worldwide. Following increased demand for remote care due to the COVID-19 pandemic, the FDA expedited its approval. Remote Check will enable hearing healthcare providers and hospitals to quickly identify those most in need of audiological care during the COVID-19 pandemic, as well as those who would benefit from Remote Check as part of their routine care over the longer term.

Remote care has been a core pillar of Cochlear's long-term innovation strategy, with access to care crucial to people who rely on a cochlear implant. With many people around the world now practising social distancing, Remote Check provides recipients with the ability to continue to access a level of care at a time when many clinics are closed to in-person visits. The FDA's expedited approval of Remote Check during the COVID-19 crisis underscores the importance of remote hearing care solutions – now more than ever – with many healthcare authorities already recognising the value in reimbursing remote care consultations for clinicians.

For recipients with a Nucleus 7 Sound Processor, Remote Check can provide significant cost savings by offering a convenient, time-saving option for care that does not require travel to a clinic. Using this technology, clinicians will not only be able to provide a more convenient care option, post the COVID-19 pandemic disruption, they can also free up time to manage the anticipated growth in the number of people needing cochlear implants, and redirect in-clinic time to manage patients with the greatest need.



Remote Check solution for cochlear implants

Convenient, at-home testing for people with a Nucleus® 7 Sound Processor

Operating and financial review

About Cochlear

For 40 years, Cochlear has been the global leader in implantable hearing solutions.

Cochlear commenced operations in 1981 as part of the Nucleus group and in 1995, listed on the Australian Securities Exchange. Today, Cochlear is a Top 50 listed Australian company with a market capitalisation of over A$12 billion.

Cochlear aims to support cochlear implantation becoming the standard of care for people with severe to profound hearing loss and provide bone conduction implants for people with conductive hearing loss, mixed hearing loss and single-sided deafness. The Company has provided more than 600,000 implant devices to people who benefit from one – or two – of the Company's implantable solutions. Whether these hearing solutions were implanted today or many years ago, Cochlear continues to bring innovative new products to market as well as sound processor upgrades for all generations of recipients.

Cochlear invests more than $180 million each year in R&D and currently participates in over 100 collaborative research programs worldwide. The global headquarters are on the campus of Macquarie University in Sydney, with regional offices in Asia Pacific, Europe and the Americas. Cochlear has a deep geographical reach, selling in over 180 countries, with a direct presence in over 30 countries and a global workforce of over 4,000 employees.

Cochlear's mission

Cochlear's mission is the passion that drives the organisation and, at a high level, focuses the strategy.

We help people hear and be heard.

We **empower** people to connect with others and live a full life.

We **transform** the way people understand and treat hearing loss.

We **innovate** and bring to market a range of implantable hearing solutions that deliver a lifetime of hearing outcomes.

Cochlear at a glance

Key products

Cochlear implants*

61%

Cochlear™ Nucleus® Profile™ Plus with Slim Modiolar Electrode (CI632)

Services*

29%

Cochlear™ Nucleus® 7 Sound Processor (CP1000)

Cochlear™ Nucleus® Kanso® 2 Sound Processor (CP950)

Acoustics*

10%

Cochlear™ Baha® 5, Baha 5 Power and Baha 5 SuperPower

Cochlear™ Osia® 2 System

Global sales

~$1.4b

in sales revenue

49% Americas*

35% EMEA*

16% Asia Pacific*

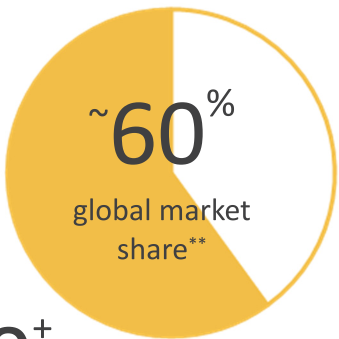
~80% Developed markets*

~20% Emerging markets*

Market leader

$180m+

in annual R&D



600,000+

implants sold***

Growing scale

4,000+

employees

100+

collaborative research programs

30+

countries with direct operations

6

key manufacturing sites

* % of sales revenue ** based on Cochlear estimates for cochlear implants *** includes cochlear and acoustic implants

Investment proposition

Cochlear provides shareholders with an opportunity to invest in the global leader in implantable hearing solutions, in an industry that has the potential to grow over the long term.

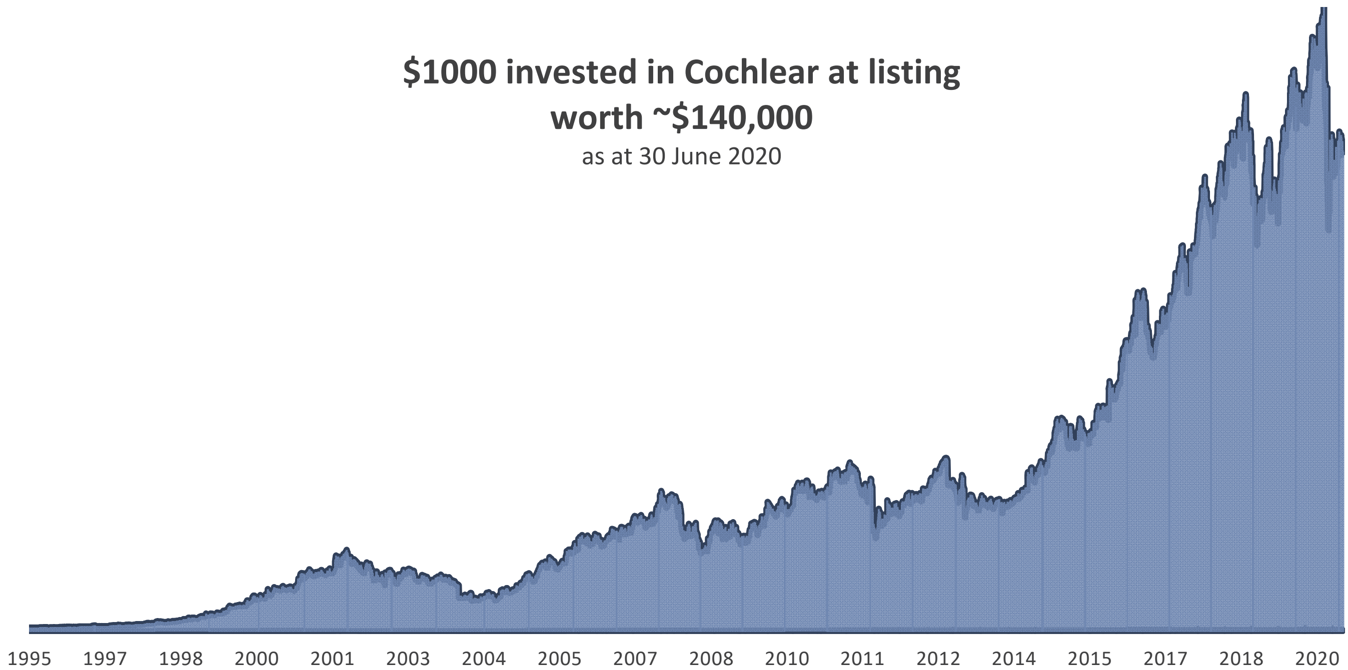
✓ **Global leader** in implantable hearing solutions for 40 years with ~60% global market share and more than 600,000 devices sold

✓ **Long-term market growth opportunity** with a significant, unmet and addressable clinical need for implantable hearing solutions and less than 5% market penetration

✓ **Unrivalled commitment to product innovation**, bringing innovative new products to market as well as sound processor upgrades for all generations of Cochlear's recipient base

✓ **Growing annuity income stream** from servicing of the expanding recipient base

✓ **Strong free cash flow generation** provides funding for market growth activities and R&D as well as the ability to reward shareholders with a growing dividend stream*



Cochlear total shareholder return since listing

*cash flow generation and dividends disrupted in FY20 by impact of COVID-19 and cost of adverse litigation outcome

Hearing loss is prevalent and under-treated

The World Health Organization estimates that there are over 460 million people worldwide – over 5% of the world's population – who experience disabling[11] hearing loss. By 2050, this is expected to rise to over 900 million people – or 1 in every 10 people.[12]

Hearing loss affects people of all ages and is particularly prevalent in people over the age of 65, with one in three people over 65 suffering a disabling hearing loss. It affects communication and can contribute to social isolation, anxiety, depression and cognitive decline.[13]

Cochlear estimates that more than 15 million people could benefit from a cochlear or bone conduction implant to treat moderate to profound hearing loss across its target segments of children globally and adults and seniors in the developed world.[14]

Cochlear's challenge, and opportunity, is that less than 5% of the people that could benefit from an implantable hearing solution are being treated.[15]

There remains a significant, unmet and addressable clinical need that is expected to continue to underpin the long-term sustainable growth of the business.

Global prevalence of hearing loss

>460 million
people globally with a disabling hearing loss

1 in 3
people over the age of 65 affected by disabling hearing loss

>15,000,000
people could benefit from a cochlear or bone conduction implant

<5%
market penetration of implantable hearing solutions

Cochlear implants a cost-effective solution

Cochlear implants provide life changing outcomes for recipients, empowering them to connect with others and live a full life. They also provide a cost-effective solution for all age groups, delivering significant returns on the investment made by the healthcare system.

Children

The estimated aggregate lifetime societal costs for a pre-lingual deaf child in developed markets is estimated to exceed US$1.5 million in 2019 dollars[16,17]. This is almost entirely attributed to reduced work productivity and/or the cost of special education.

Once lifetime medical costs are excluded from the total costs, it is estimated that the return on investment of a cochlear implantation for a pre-lingual deaf child is 13.5:1, meaning each dollar spent on a cochlear implant has the potential to result in up to $13.5 in return to society[18].

Estimated lifetime societal costs for a pre-lingual deaf child in developed markets exceeds US$1.5 million

Adults

The aggregate societal costs of an adult with severe to profound hearing loss is estimated to range between US$702,000 (for those under 45 years of age) and US$392,000 (for those between 45 and 65 years of age) in 2019 dollars. These societal costs are driven almost exclusively by reduced work productivity.

One study reported that when compared to those with normal hearing, adults with hearing loss were reported to be more than three times more likely to have low educational attainment and were almost twice as likely to be unemployed or under employed[20].

In another study, individuals with severe and profound hearing loss were also found to earn approximately 77% of the average income of those with mild hearing loss. The lost income due to untreated hearing loss has even greater socioeconomic implications when consideration is given to the value of unrealised taxes associated with this lost income[21].

The effective use of implants is cost-effective in adults and seniors with an estimated return on investment of 10:1

Seniors

Dementia and other cognitive decline diseases are some of the costliest conditions to treat in the world[22]. The estimated worldwide cost of dementia was predicted to reach US$1 trillion in 2018 – rapidly rising to US$2 trillion by 2030. The number of affected individuals is predicted to almost double every 20 years[23].

Unfortunately, individuals with severe hearing loss are almost five times more likely to develop dementia than people without hearing loss[24].

The effective use of hearing aids and implants is cost-effective and has been proven in adults and seniors with an estimated return on investment of 10:1[25].

Growing demand for cochlear implants

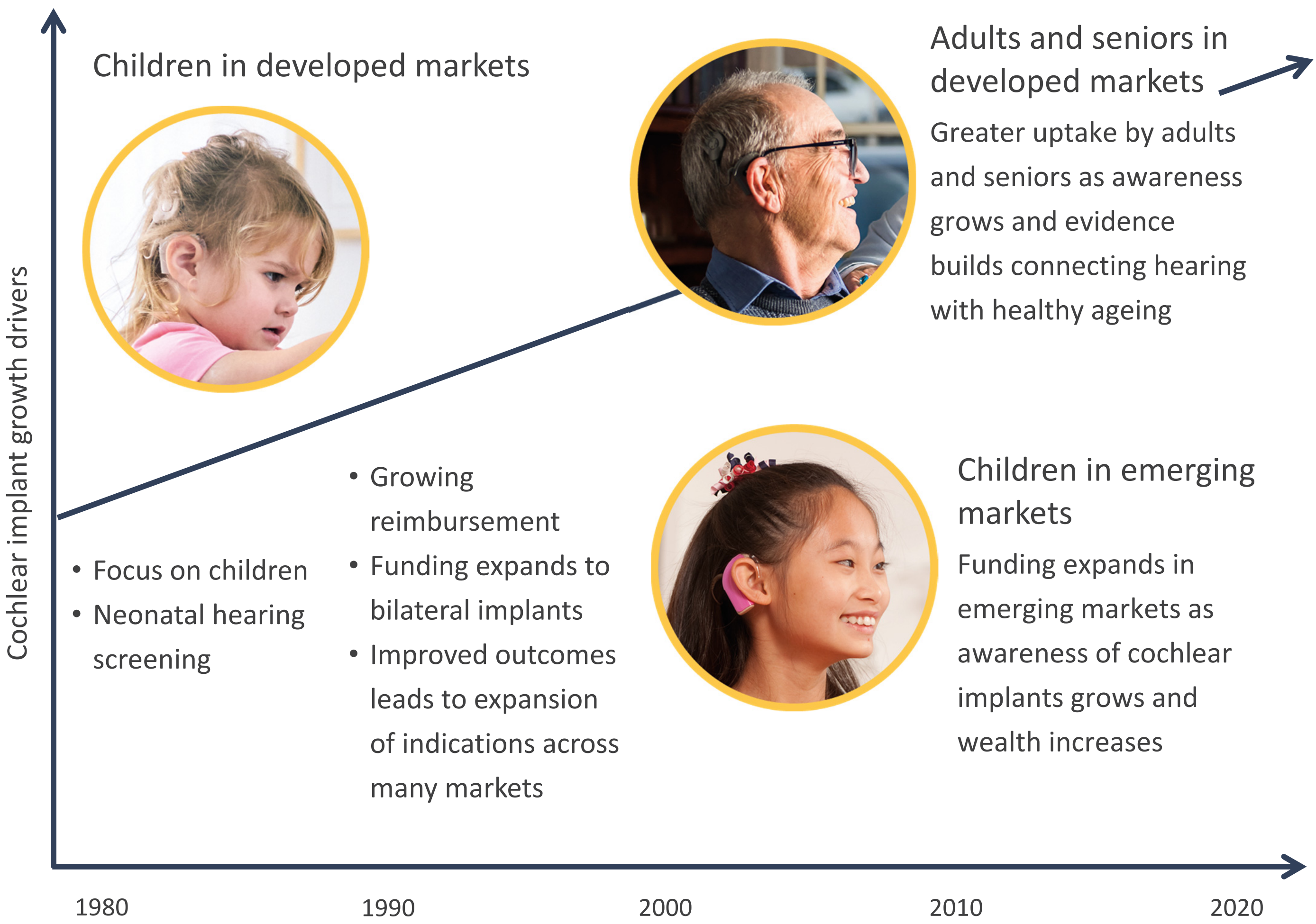
Demand for cochlear implants is increasingly being driven by older adults in developed markets and by children across the emerging markets.

Cochlear implants started as a solution for people with a profound hearing loss, equivalent to a hearing loss of greater than 90 decibels (dB), almost 40 years ago. Adoption of cochlear implantation for children grew rapidly, driven by the widespread implementation of neonatal hearing screening which allowed for early detection of hearing loss in newborns. Today, cochlear implantation has become the standard of care for newborns across the developed markets.

Cochlear's multi-decade investment in innovation has materially improved the hearing outcomes provided by cochlear implants, improving the quality of life of recipients. It has also driven the expansion of indications for the implants in many countries to include people with lower levels of hearing loss, which has seen the addressable market for cochlear implants grow significantly.

Over the last 10 years, there has been a greater uptake of cochlear implantation by older adults, particularly seniors, as awareness of the intervention has grown, and the body of evidence builds connecting good hearing with healthy ageing. At the same time, funding has expanded in emerging markets as awareness of cochlear implants grows and wealth increases, driving implantation of children across the emerging world.

Growth is shifting to under-penetrated segments



Strategic priorities

To achieve its mission, Cochlear aims to support cochlear implantation becoming the standard of care for people with severe to profound hearing loss and provide bone conduction implants for people with conductive hearing loss, mixed hearing loss and single-sided deafness.

Cochlear is committed to maintaining its technology leadership position in the industry by investing in R&D to improve hearing outcomes and expand the indications for implantable solutions. We aim to grow the hearing implant market by growing awareness and access for implant candidates. And with a growing recipient base, Cochlear is actively strengthening its servicing capability to provide products, programs and services to support the lifetime relationship with recipients.

Cochlear's strategic priorities

Retain market leadership

Market-leading technology I World-class customer experience

Grow the hearing implant market

Awareness I Market access I Clinical evidence

Deliver consistent revenue and earnings growth

Invest to grow I Operational improvement I Strong financial position

For an in-depth review of Cochlear's strategy and financial history, please refer to the Strategy Overview which is available at www.cochlear.com.

Operational review

Product and service highlights

$m	2020	2019	Change % (reported)	Change % (CC)*	Sales mix
Cochlear implants (units)	31,662	34,083	⬇ 7%		
Sales revenue					
Cochlear implants	817.9	845.1	⬇ 3%	⬇ 8%	61%
Services (sound processor upgrades and other)	395.5	427.2	⬇ 7%	⬇ 12%	29%
Acoustics	138.9	173.8	⬇ 20%	⬇ 24%	10%
Total sales revenue	**1,352.3**	**1,446.1**	⬇ **6%**	⬇ 11%	**100%**

* Constant currency (CC) removes the impact of exchange rate movements and foreign exchange (FX) contract gains/(losses) to facilitate comparability. See Notes on page 28 for further detail.

Cochlear implants

Cochlear implant units declined 7% with first half units up 13% and second half units down 26%.

In the first half, cochlear implant units increased 13% as the Nucleus Profile Plus Series cochlear implant was launched across major markets. The new implant has been well-received by professionals and consumers with improvements in market share experienced across many markets.

From January to mid-March, cochlear implant volumes across the developed markets were tracking in line with expectations. However, from mid-March we experienced a substantial, short-term negative impact on cochlear implant surgeries, particularly in the US and Western Europe, as healthcare systems diverted resources to meet the increasing demands of managing COVID-19.

In April, cochlear implant unit sales across the developed markets declined by around 80% (compared to April 2019), with most elective surgeries postponed. To the extent there were surgeries, they were predominantly for children.

Surgeries recommenced across many markets from early-May. Market conditions however still varied across our developed markets by the end of June with surgery volumes recovering relatively quickly in the US, Germany, Benelux and Australia and more slowly in the UK, Spain and Italy. By the end of June, over 80% of cochlear implant surgical centres in the developed markets had recommenced surgeries.

Emerging markets, which represent around 20% of cochlear implant revenue, delivered a strong start to the year with volumes up over 20% in the first half. January/February volumes were weaker as surgeries were delayed in China, Cochlear's largest emerging market, due to COVID-19. Surgeries recommenced in China in March and have recovered quickly. Surgeries in China continue to grow as a result of the market opportunity and investments we have made to expand our presence over the last few years. Surgeries however across most other markets, including India and Latin America, have remained very low as COVID-19 cases continue to grow.

Services (sound processor upgrades and other)

Services revenue declined 7% (12% in CC) with first half revenue up 9% and second half revenue down 23%.

Services were materially impacted by COVID-19 in the fourth quarter of FY20. While some recipients have been able to access sound processor upgrades remotely, clinic closures have delayed access to sound processor upgrades for many people.

Cochlear's remote servicing capability, with tools including Cochlear™ Link and Remote Check, are assisting clinicians and recipients with performance, mapping, and troubleshooting in markets where they are approved. Many countries and clinics have been adapting, enabling greater levels of remote access and programming to assist recipients unable to visit clinics as a result of COVID-19. In recognition of the importance of providing support, the FDA fast-tracked approval of Remote Check in April.

Acoustics

Acoustics revenue declined by 20% (24% in CC) with first half revenue down 9% and second half revenue down 32%.

In the first half, we experienced some loss of market share from competitor product launches. The market also slowed more than expected in anticipation of the launch of the next generation bone conduction implant, the Cochlear™ Osia® 2 System, which commenced its rollout in the US in February. Like cochlear implants, the second half was materially impacted by COVID-19 due to the delay of elective surgeries.

Acoustics revenue is largely generated from the US and the UK. Surgery volumes have improved in the US since May with increasing demand for the Osia 2 System. Acoustic implant surgeries in the UK, however, have not yet restarted following the COVID-19 shutdowns.

Regional review

$m	2020	2019	Change % (reported)	Change % (CC)	Sales mix
Americas	650.3	688.6	⬇ 6%	⬇ 11%	49%
EMEA	479.6	519.2	⬇ 8%	⬇ 11%	35%
Asia Pacific	222.4	238.3	⬇ 7%	⬇ 10%	16%
Total sales revenue	**1,352.3**	**1,446.1**	**⬇ 6%**	**⬇ 11%**	**100%**

Americas (US, Canada and Latin America)

Sales revenue declined by 6% (11% in CC) with the first half up 9% and second half down 21%.

H1: The Americas had a solid start to the year with strong cochlear implant revenue growth moderated by low growth in Services revenue and a decline in Acoustics revenue. The launch of the Nucleus Profile Plus Series cochlear implant in the US in late June 2019 was well-received by the market, driving an uplift in market share throughout the year.

Services revenue in the US was flat in the first half as the business cycled very strong sales in HY19, with penetration rates reaching high levels. Acoustics sales declined with some loss of share from competitor product launches and a slowdown in surgeries in anticipation of the launch of the Osia 2 System.

H2: Second half revenue for the Americas declined by 21% (26% in CC), materially impacted by the elective surgery deferrals from mid-March. Surgeries have started to recommence across North America with clinics progressively reopening. There are still very few surgeries in Latin America as COVID-19 infection rates continue to rise. The decline in Latin American implant revenue has been partly offset by growth in Services revenue.

EMEA (Europe, Middle East and Africa)

Sales revenue declined by 8% (11% in CC) with the first half up 6% and second half down 20%.

H1: EMEA delivered strong cochlear implant revenue growth in the first half moderated by low growth in Services revenue and a decline in Acoustics revenue.

Like the US, Services revenue growth slowed in the first half as the business cycled very strong sales in HY19, with penetration rates reaching high levels and Acoustics revenue declined. EMEA’s emerging markets grew in the first half as a result of the timing of a number of tenders, underpinned by investments in the organisation in recent years.

H2: Second half revenue for EMEA declined by 20% (23% in CC), as a result of the deferral of elective surgery from mid-March. Surgery volumes across Western Europe started improving during May with significant variability across countries. Germany and Benelux have recovered quickly while the UK, Italy and Spain continue to record a small, but growing number of surgeries.

Asia Pacific (Australasia and Asia)

Sales revenue declined by 7% (10% in CC) with the first half up 18% and second half down 29%.

H1: In the first half, Japan and South Korea experienced strong growth across both cochlear implant units and sound processor upgrades. China recorded strong growth in sales revenue, benefiting from increased investment in sales and marketing capability over the past few years.

H2: Second half revenue declined by 29% (32% in CC) as a result of the impact of the deferral of elective surgeries which varied greatly by country. China has recovered quickly and is growing strongly. South Korea delivered strong growth in FY20 with Cochlear gaining share in a market that continued to conduct elective surgeries throughout the pandemic. Australia and China delivered solid growth in Services revenue. India however continues to experience high infection rates from COVID-19 with very few surgeries since April.

Financial review

Profit and loss

$m	2020	2019	Change % (reported)	Change % (CC)**
Sales revenue	**1,352.3**	**1,446.1**	**(6%)**	**(11%)**
Cost of sales	344.4	351.1	(2%)	(5%)
% gross margin	*75%*	*76%*	*(1) pt*	*0 pts*
Selling, marketing and general expenses	470.0	450.9	4%	0%
Research and development expenses	185.1	184.4	0%	(1%)
% of sales revenue	*14%*	*13%*	*1 pt*	*(1) pt*
Administration expenses	93.8	94.8	(1%)	(1%)
Operating expenses	**748.9**	**730.1**	**3%**	**0%**
Other income / (expenses)	(20.4)	13.8		
FX contract losses	(31.7)	(19.4)		
EBIT (underlying)*	**206.9**	**359.3**	**(42%)**	**(42%)**
% of sales revenue	*15%*	*25%*		
Net finance expense	8.9	4.5	98%	
Income tax expense*	44.2	88.9	(50%)	
% effective tax rate	*22%*	*25%*		
Net profit (underlying)*	**153.8**	**265.9**	**(42%)**	**(42%)**
*% net profit margin**	*11%*	*18%*		
Innovation fund gains after-tax	24.2	10.8		
Patent litigation expense after-tax	(416.3)	-		
Net profit / (loss) (reported)	**(238.3)**	**276.7**	**(186%)**	**(187%)**

* Excluding innovation fund gains and patent litigation expense

** Constant currency (CC) removes the impact of exchange rate movements and FX contract gains/(losses) to facilitate comparability. See Notes on page 28 for further detail.

Sales revenue declined by 6% (11% in CC) to $1,352.3 million, with revenue up 9% in the first half and down 22% in the second half. Underlying net profit declined 42% to $153.8 million due to the rapid fall in sales in the second half, a consequence of COVID-19-related surgery deferrals and clinic closures. After factoring in patent litigation expenses and innovation fund gains, Cochlear recorded a net loss of $238.3 million for FY20.

Key points of note:

- Cost of sales declined by 2% (5% in CC) to $344.4 million, reflecting declining sales in the fourth quarter. The gross margin declined by 1 percentage point to 75%. Gross margin benefited from lower warranty costs, the result of improved sound processor manufacturing and design that has resulted in lower warranty repairs. This benefit was offset by the impact of lower overhead recovery arising from lower manufacturing volumes since May;
- Selling, marketing and general expenses increased by 4% (0% in CC) to $470.0 million, with the first half up 9% in CC and the second half down 8%. Continued investment was made in market growth activities including direct-to-consumer marketing, standard of care and market access initiatives. The second half decline reflects actions to limit all non-essential spending from mid-March and includes a hiring freeze and temporary pay reductions for the Board and senior management across the business in the fourth quarter. These savings were partially offset by a $10.0 million increase in the doubtful debts provision resulting from higher collections risk associated with COVID-19;
- Investment in R&D was in line with FY19 (down 1% in CC) at $185.1 million, representing 14% of sales revenue;
- Operating expenses include a $23.6 million benefit from the suspension of short-term incentive payments;
- FX contract losses increased by $12.3 million to $31.7 million as a result of the weaker Australian dollar against major trading currencies;
- Net finance expenses increased by 98% to $8.9 million and includes $6.1 million in interest expense resulting from the adoption of new leasing accounting standard AASB16. Net finance expenses (excluding the lease-related expense) declined by 38% to $2.8 million with the business benefitting from lower interest rates and interest on cash deposits from the March capital raising;
- $24.2 million in innovation fund gains after-tax includes a $25.0 million gain from the revaluation of the Nyxoah shareholding and $0.8 million in equity accounted losses; and
- $416.3 million in patent litigation expenses after-tax relates to an adverse litigation judgment in the long-running AMF patent infringement case. $420.1 million was paid in June and a provision was made for US$75 million in prejudgment interest and attorneys' fees with payment conditional upon the outcome of an appeal by Cochlear to the US Supreme Court.

Other expenses

$m	2020	2019	Change
Government assistance (COVID-19-related)	23.6	-	23.6
Release in the contingent consideration (Sycle)	13.2	10.8	2.4
Ineffective forward exchange contracts	(26.1)	-	(26.1)
Carina write-down	(17.3)	-	(17.3)
Otoconsult NV write-down	(12.5)	-	(12.5)
Other	(1.3)	3.0	(4.3)
Other income / (expenses)	**(20.4)**	**13.8**	**(34.2)**

The Profit & loss includes other expenses of $20.4 million, which are largely one-off in nature, including:

- Due to the impact of COVID-19, Cochlear has received $23.6 million in government assistance through the US Coronavirus Aid, Relief and Economic Security Act (CARES Act), Australia's JobKeeper Program and other assistance programs offered in Europe and Asia;
- $13.2 million non-cash benefit related to the final release in the contingent consideration value of Sycle;
- $26.1 million in expenses relating to ineffective forward exchange contracts, predominantly FY21 USD contracts, due to the combined effects of COVID-19 and the adverse litigation judgment on the probable foreign currency cash flows anticipated to be received during that period. As a result, those cash flow hedges no longer met the criteria for hedge accounting and were closed;
- $17.3 million in the write-down of assets associated with the Carina acoustic implant following the decision to cease sales of the product due to low volumes; and
- $12.5 million in the write-down of assets and licencing costs associated with Otoconsult NV following the decision to pursue the development of different AI-assisted mapping in-house.

Cash flow

$m	2020	2019	Change
EBIT (underlying)	206.9	359.3	(152.4)
Depreciation and amortisation (excl AASB16 impact)	49.1	38.5	10.6
Depreciation and amortisation (AASB16-related)	28.4	-	28.4
Changes in working capital and other	66.9	(6.6)	73.5
Cash impact of patent litigation expense	(420.1)	-	(420.1)
Net interest paid	(8.9)	(4.5)	(4.4)
Income taxes paid	(80.1)	(90.7)	10.6
Operating cash flow	**(157.8)**	**296.0**	**(453.8)**
Capital expenditure	(111.4)	(86.6)	(24.8)
Acquisition of other intangible assets	(19.1)	(28.0)	8.9
Other net investments	(14.2)	(23.2)	9.0
Free cash flow	**(302.5)**	**158.2**	**(460.7)**
Proceeds from issue of shares	1,081.9	7.4	1,074.5
Dividends paid	(193.7)	(181.8)	(11.9)
Payment of lease liability & other	(25.7)	(0.6)	(25.1)
Change in net debt – decrease / (increase)	**560.0**	**(16.8)**	**576.8**

Free cash flow declined by $460.7 million to be an outflow of $302.5 million, driven by payment of costs associated with an adverse litigation judgment in June and the impact on earnings from the COVID-19-related fall in revenue during the fourth quarter. Cochlear's financial position was bolstered by the $1.1 billion capital raising in March which resulted in net debt declining by $560.0 million, more than offsetting the decline in free cash flow.

Key points of note:

- EBIT (underlying) declined by $152.4 million as a result of the significant decline in sales revenue in the fourth quarter;
- $420.1 million in cash impact of patent litigation expenses reflects the payment of damages and post judgment interest associated with an adverse litigation judgment in June;
- Changes in working capital and other of $66.9 million reflects the benefit of the reduction in trade receivables resulting from lower sales revenue in the fourth quarter;
- The $10.6 million reduction in income taxes paid reflects the impact of COVID-19 during the second half. The tax credit resulting from the patent litigation expenses will result in lower tax payments in FY21;
- Capital expenditure (capex) increased by $24.8 million to $111.4 million, reflecting stay in business capex, the continued development of the China manufacturing facility, fitout of the new, larger Denver office and IT platform development;
- The acquisition of intangible assets includes the licencing of a range of R&D-related assets; and
- Other net investments primarily relate to the additional investment made in Nyxoah.

Capital employed

$m	2020	2019	Change
Trade receivables	211.4	299.5	(88.1)
Inventories	223.8	195.4	28.4
Less: Trade payables	(155.3)	(160.8)	5.5
Working capital	**279.9**	**334.1**	**(54.2)**
Working capital / sales revenue	*21%*	*23%*	
Property, plant and equipment	230.5	166.5	64.0
Intangible assets	410.3	424.4	(14.1)
Investments (including equity accounted)	94.9	47.8	47.1
Other net liabilities	(71.1)	(143.9)	72.8
Capital employed	**944.5**	**828.9**	**115.6**

Capital employed increased by $115.6 million to $944.5 million since June 2019 reflecting an increase in property, plant and equipment and other net liabilities and a reduction in working capital.

Key points of note:

- Trade receivables reduced by $88.1 million, a consequence of the reduced sales revenue;
- Inventories increased by $28.4 million, a consequence of the reduced sales revenue and a decision to build inventory levels to enable the business to cater to demand as surgeries recommence;
- Property, plant and equipment increased by $64.0 million and includes the investment in the China manufacturing facility and fitout of the new Denver office;
- The increase in investments includes a $35.8 million pre-tax increase in the value of Cochlear's investment in Nyxoah;
- Other net liabilities decreased by $72.8 million to $71.1 million reflecting movements across a number of other assets and liabilities. Net current tax assets increased by $84.8 million reflecting refundable FY20 tax payments. Tax losses resulting from the patent litigation expense and COVID-19 impacts were incurred late in the year, resulting in an overpayment of tax instalments for the year. The $85.9 million increase in provisions primarily reflects the US$75 million provision for prejudgment interest and attorneys' fees with payment conditional upon the outcome of an appeal by Cochlear to the US Supreme Court. A $25.5 million reduction in net FX contract liabilities represents the mark-to-market value of all FX hedging contracts as at 30 June 2020.

Net debt

$m	2020	2019	Change
Loans and borrowings:			
Current	393.1	3.3	389.8
Non-current	79.9	178.3	(98.4)
Total loans and borrowings	**473.0**	**181.6**	**291.4**
Less: Cash, cash equivalents and term deposits	(930.0)	(78.6)	(851.4)
Net debt / (cash)	**(457.0)**	**103.0**	**(560.0)**
Facility limit	1,003.8	414.5	589.3
Debt drawn	473.9	182.4	291.5
Balance remaining	529.9	232.1	297.8

Net debt declined by $560.0 million, resulting in a net cash position of $457.0 million. Cochlear's liquidity position has increased as a result of a $1.1 billion capital raising in March and expanded debt facilities. Combined net cash and undrawn debt facilities total $986.9 million as at 30 June.

Dividends

$m	2020	2019	Change %
Interim ordinary dividend (per share)	$1.60	$1.55	3%
Final ordinary dividend (per share)	-	$1.75	(100%)
Total ordinary dividends (per share)	**$1.60**	**$3.30**	**(52%)**
% payout ratio (underlying)	60%	72%	
% franking	100%	100%	

In March, Cochlear announced the suspension of the dividend until trading conditions improve. As a result, no final dividend has been declared. Full year dividends declined by 52% to $1.60 per share, representing a payout of 60% of underlying net profit. The Board expects to resume payment of a dividend once a clear and sustained improvement in sales revenue has been established and cash flow generation is sufficient to support its resumption.

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.

Non-International Financial Reporting Standards (IFRS) financial measures

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 contract losses on hedged sales. Given the significance of foreign 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

$m	2020	2019	Change %
Net profit (underlying)	**153.8**	**265.9**	**(42%)**
FX contract movement		(38.4)	
Spot exchange rate effect to sales revenue and expenses*		37.9	
Balance sheet revaluation*		(2.4)	
Net profit (underlying) (CC)	**153.8**	**263.0**	**(42%)**
Patent litigation expense and innovation fund gains after-tax	(392.1)	10.8	
Net profit (reported) (CC)	**(238.3)**	**273.8**	**(187%)**

* FY20 actual v FY19 at FY20 rates.

Business risks

Cochlear has a sound and robust Risk Management Framework to identify, assess and appropriately manage risks. Details of Cochlear's Risk Management Framework can be found in the 2020 Corporate Governance Statement, which is available on the website.

Cochlear's principal business risks are outlined below. These are significant risks that may materially adversely affect the business strategy, financial position or future performance. It is not possible to identify every risk that could affect Cochlear's business, and the actions taken to mitigate these risks cannot provide absolute assurance that a risk will not materialise.

Risk	Description and potential consequences	Strategies used by Cochlear to mitigate the risk
Pandemic	As COVID-19 has demonstrated, pandemics have the potential to impact our markets as elective surgeries may be deferred in order to reduce the strain on healthcare systems. Travel restrictions, government mandated shutdowns and potential supply chain impacts could also have adverse consequences to our business.	Cochlear has well-developed business continuity and crisis management plans, a diverse range of customers and a range of products and services that serve to mitigate or manage the impact a pandemic may have on our business.
Product innovation and competition	Cochlear is exposed to the risk of failing to develop and produce innovative products for customers. Increased competition exposes Cochlear to the risk of losing market share as well as a decrease in average selling prices in the industry. Cochlear is also exposed to the risk of medical, biological and/or technological advancement by third parties where alternative products or treatments are developed and commercialised that render Cochlear's products obsolete for future candidates. This could result in a loss of new business.	In FY20, Cochlear invested 14% of sales revenue in R&D. Cochlear also works with over 100 external research partners. The creation of new intellectual property and the protection of new and existing intellectual property are a key focus for Cochlear. Cochlear has plans to launch a series of new products across all categories of the business over the coming years, focused on both market share and market growth. Cochlear also has a practice of identifying and assessing potential disruptive technologies.
Infringement litigation	Cochlear operates in an industry that has substantial intellectual property and patents, designs and trademarks protecting that intellectual property. Cochlear is exposed to the risk of litigation for alleged infringement. This could result in Cochlear paying royalties to be able to continue to manufacture product or paying damages and/or receiving injunctions preventing Cochlear selling products it had developed.	Cochlear has a comprehensive patent portfolio across its technologies. Cochlear conducts freedom to operate searches as part of its internal processes before launching new products. Cochlear utilises internal and external legal resources to manage any litigation issues.
Misappropriation of know-how and intellectual property	Cochlear is exposed to the risk of its know-how and intellectual property being misappropriated either through hacking of its systems or by employees, consultants and third parties who from time to time have access to Cochlear's know-how and intellectual property. This could result in competitors using this information and increasing their competitiveness. Cochlear could lose market share as a result.	Cochlear monitors its key systems and database, for inappropriate access from both internal and external sources. Confidentiality agreements are in place with key employees and third parties that are exposed to Cochlear's know-how and intellectual property.

Risk	Description and potential consequences	Strategies used by Cochlear to mitigate the risk
Medical device regulations	Cochlear operates in a highly regulated industry. Medical devices are subject to strict regulations, including data security, of regulatory bodies in the US, Europe, Asia and Australia as well as many other local bodies in countries where Cochlear's products are sold. Regulatory bodies periodically perform audits at Cochlear's manufacturing and distribution sites. If Cochlear or a third-party supplier fails to satisfy regulatory requirements or the regulations change and modifications are not made, this could result in the imposition of sanctions or Cochlear's products being subject to recall and/or the loss of sales and reputational harm. Changes to medical device regulations or delays in achieving regulatory approval can impact Cochlear's ability to sell its products.	Cochlear has a worldwide quality assurance system in place. Regulatory requirements and changes in the regulatory environment are actively monitored and assessed.
Reimbursement	The majority of Cochlear's customers rely on a level of reimbursement from insurers and government health authorities to fund their purchases. There is increasing pressure on healthcare budgets globally which may lead to pressure on reimbursed prices. Cochlear may also be subject to healthcare-related taxes imposed by government agencies and this could negatively impact the ability of candidates to access Cochlear's products.	Cochlear continues to work with reimbursement and government agencies throughout the world to emphasise the health and economic benefits and cost effectiveness of intervention to restore or improve hearing.
Product liability	The manufacturing, testing, marketing and sale of Cochlear's products involve product liability risk. As the developer, manufacturer, marketer and distributor of certain products, Cochlear may be held liable for damages arising from use of its products during development or after the product has been implanted.	Cochlear maintains product liability insurance and operates a worldwide quality assurance system related to the design, testing, manufacture and post-market monitoring of its products.
Interruption to product supply	Cochlear relies on third-party suppliers for the supply of key materials and services. This carries the risk of delays and disruptions in supplies. Certain materials are available from a single source only and regulatory requirements make substitution costly, time-consuming or commercially unviable. Cochlear manufactures its latest generation products across five sites globally. There is the potential risk of disruption to sales should a manufacturing facility be unable to operate. Any new manufacturing facility will require regulatory approval prior to being able to produce and sell product made at this facility. This approval could take many months or years.	Cochlear monitors its suppliers and identifies potential second-source supply. Inventories are managed and purchased in sufficient quantities for continued product supply in the short term. Where appropriate, lifetime buys, strategic raw materials purchases, and supply chain interventions are made. Cochlear also regularly reviews its disaster recovery plans for its manufacturing sites and maintains business interruption insurance.

Risk	Description and potential consequences	Strategies used by Cochlear to mitigate the risk
Political, economic or social instability	Cochlear sells in over 180 countries. Several of the markets include significant tender sales. The future outcome of tender sales is uncertain. Regional political, economic or social instability could negatively impact sales and the receipt of payment for sales. Economic cycles could also impact negatively on the healthcare industry, including within the hearing healthcare sector.	Cochlear assesses the countries it sells into and does not have a significant concentration of sales in countries impacted by material political, economic or social instability. Cochlear utilises global scanning software to assess partners, distributors and suppliers against sanctions checklists on an ongoing basis. Cochlear conducts and promotes research into the economic benefits of hearing health.
Foreign exchange rates	Cochlear is exposed to currency risk on sales and purchases that are denominated in a currency other than the respective functional currencies of the legal entities. The currencies in which these transactions primarily are denominated are Australian dollars (AUD), US dollars (USD), Euros (EUR), Japanese yen (JPY), Sterling (GBP), Swedish kroner (SEK) and Swiss francs (CHF). Over 90% of Cochlear's revenues and over 50% of costs are denominated in currencies other than AUD.	Currency risk is hedged in accordance with the Board approved treasury risk policy. The treasury risk policy aims to manage the impact of short-term fluctuations on Cochlear's cash flow. Over the longer term, permanent changes in market rates will have an impact on earnings. Derivative financial instruments (forward exchange contracts) are used to hedge exposure to fluctuations in foreign exchange rates in a declining level of cover out to three years.
Credit	Cochlear's exposure to credit risk is influenced by the geographical location and characteristics of individual customers. Cochlear does not have a significant concentration of credit risk with a single customer. Most significant debtors are governments, government-supported universities and clinics or major hospital chains.	Policies and procedures for credit management and administration of receivables are established and executed at a regional level. In monitoring customer credit risk, the ageing profile of total receivables balances and individually significant debtors is reported by geographic region to the Board on a monthly basis. Regional management is responsible for identifying high risk customers and placing potential restrictions on future trading, including suspending future shipments and administering dispatches on a prepayment basis. In addition, where appropriate, absolute country limits are in place and Chief Financial Officer approval is required to increase a limit. These limits are periodically reviewed by the Audit & Risk Committee.

Risk	Description and potential consequences	Strategies used by Cochlear to mitigate the risk
Operations	Operational risk is the risk of direct and indirect loss arising from a wide variety of causes associated with Cochlear's processes, personnel (including executive transitions), technology and infrastructure and generally accepted standards of corporate behaviour. Operational risks arise from Cochlear's operations. These risks could result in the loss of sales and reputational harm.	Standards for the management of operational risk are in place in the following key areas: • Requirements for appropriate segregation of duties, including the independent authorisation of transactions; • Requirements for the reconciliation and monitoring of transactions; • Appropriate insurance programs; • Documentation of controls and procedures; • Requirements for the periodic assessment of operational risks faced, and the adequacy of controls and procedures to address the risks identified; • Internal and external audit programs; • Development of contingency plans; • Succession planning for key management personnel; • Training and professional development; • Employee health and safety programs; and • Ethical and business standards.
Information security	Cochlear handles and stores personal information, including health information, for its customers and employees. With expanding information privacy and security regulations, and an increasingly hostile cyber environment, Cochlear recognises information privacy and cyber security as an increasing risk.	Cochlear regularly assesses its information governance and cyber security controls in light of emerging technological threats and expanding privacy laws. These assessments are used to determine any appropriate corrective actions and improvements. In addition to the ongoing assessment and remediation of operational privacy and security activities, Cochlear maintains cyber insurance as part of its overall risk mitigation strategy for information privacy and security risk.
Talent management	Cochlear operates in a very competitive environment, particularly in relation to attracting scientific talent into the group.	Talent management programs are in place, both within Australia and in our key international markets.
Corporate governance	Cochlear operates either directly or indirectly in most countries in the world. As such, it is exposed to risks related to general corporate governance compliance issues (e.g. tax, customs, local regulations). These risks could result in regulatory fines or reputational damage.	Cochlear has a system of controls in place to mitigate such corporate governance risks, including regular regional and country reporting on any potential issues. A Global Code of Conduct and other regional policies are in place to ensure all staff are appropriately trained and aware of the need to comply with all corporate requirements.

Board of directors

Rick Holliday-Smith

Chairman Age 70

Appointed to the Board 1 March 2005: Chairman of the Nomination Committee. Member of the Audit & Risk and People & Culture Committees.

Background: Global executive and leadership experience in capital markets and derivatives, and a background in venture capital activities. Former President of NationsBank-CRT, Chicago and Managing Director of Hong Kong Bank Limited, London.

Other boards: Chairman, ASX Limited. Non-executive Chairman, QBiotics and member of the Macquarie University Faculty of Business and Economics Advisory Board.

Former directorships: Chairman, Snowy Hydro Limited and SFE Corporation Limited. Director, Servcorp Limited, St George Bank Limited, Exco Resources NL, DCA Group Limited and MIA Group Limited.

Qualifications: BA (Hons), FAICD, CA

Dig Howitt

CEO & President and Managing Director Age 53

Appointed to the Board 14 November 2017 and as CEO & President 3 January 2018: Member of the Medical Science and Technology & Innovation Committees.

Background: Joined Cochlear in 2000 and has a wealth of experience across the Company in roles including Chief Operating Officer, SVP, Manufacturing and Logistics and President, Asia Pacific. Prior to joining Cochlear, worked for Boral and Boston Consulting Group. Dig is a member of the Male Champions of Change STEM group. Appointed as President of Cochlear on 31 July 2017 and became CEO & President on 3 January 2018.

Qualifications: BE (Hons), MBA

Yasmin Allen

Non-executive Director Age 56

Appointed to the Board 2 August 2010: Chairman of the Audit & Risk Committee. Member of the People & Culture, Nomination and Technology & Innovation Committees.

Background: Extensive career in investment banking with senior roles in strategic analysis and corporate advice. Former Vice President of Deutsche Bank AG.

Other boards: Chair of Australian Federal Government Steering Group for Digital Technology Pilot. Director, Santos Limited, ASX Limited and National Portrait Gallery. Member of the George Institute for Global Health Board. Chairman, Advance (Global Australian Network), Acting President, Australian Government Takeovers Panel, Chairman, Faethm.org and Chair, Australian Federal Government Steering Group for Digital Technology Pilot.

Former directorships: Director, Insurance Australia Group Limited. National director of the Australian Institute of Company Directors. Member of The Salvation Army Advisory Board. Chair of Macquarie Specialised Asset Management. Director, ANZ Investment Bank and Associate Director, HSBC London.

Qualifications: BCom, FAICD

Andrew Denver

Non-executive Director Age 71

Appointed to the Board 1 February 2007: Member of the Audit & Risk, Medical Science, Technology & Innovation and Nomination Committees.

Background: Extensive experience in the life sciences industry. Former Managing Director of Memtec Limited and President Asia for Pall Corporation.

Other boards: Chairman, SpeeDx and Director, Vaxxas and QBiotics.

Former directorships: Executive Chairman, Universal Biosensors.

Qualifications: BSc (Hons), MBA, FAICD

Donal O'Dwyer

Non-executive Director Age 67

Appointed to the Board 1 August 2005: Member of the Audit & Risk, Medical Science, Nomination and Technology & Innovation Committees.

Background: Executive experience in global general management of healthcare products and medical devices. Former worldwide President of Cordis Cardiology (a Johnson & Johnson company) and President of Baxter's Cardiovascular Group, Europe.

Other boards: Director, Mesoblast Limited, Fisher & Paykel Healthcare and NIB Holdings Ltd. Chairman of Endoluminal Sciences and Director Cordis Asset Management Pty Ltd.

Former directorships: Chairman, CardieX (formerly Atcor Medical).

Qualifications: BE Civil, MBA

Glen Boreham, AM

Non-executive Director Age 56

Appointed to the Board 1 January 2015: Chairman of the People & Culture Committee. Member of the Audit & Risk, Nomination and Technology & Innovation Committees.

Background: Led organisations in information technology, new media and the creative industries through periods of rapid change and innovation. Former Managing Director of IBM Australia and New Zealand.

Other boards: Director, Southern Cross Media Group and Link Group. Chairman, Advisory Board IXUP.

Former directorships: Director of Data#3. Chairman of Screen Australia, Advance (Global Australian Network), Business School and Industry Advisory Board for the University of Technology, Sydney.

Qualifications: BEc, FAICD

Alison Deans

Non-executive Director Age 52

Appointed to the Board 1 January 2015: Chairman of the Technology & Innovation Committee. Member of the Audit & Risk, Nomination and People & Culture Committees.

Background: Extensive experience leading technology-enabled businesses across e-commerce, media and financial services. Former Chief Executive Officer of netus, Hoyts Cinemas, ecorp and eBay Australia and New Zealand.

Other boards: Director, Westpac Banking Corporation, Ramsay Health Care Limited and Deputy Group Pty Ltd. Senior Advisor to McKinsey & Company. Member of Investment Committee, CSIRO Innovation fund (Main Sequence Ventures) and Director of SCEGGS Darlinghurst Limited and The Observership Program.

Former directorships: Director of Insurance Australia Group Limited, Social Ventures Australia and kikki.K Holdings Pty Ltd. Chairman of ninemsn, Allure Media and Downstream Media.

Qualifications: BA, MBA, GAICD

Prof Bruce Robinson, AC

Non-executive Director Age 63

Appointed to the Board 13 December 2016: Chairman of Medical Science Committee. Member of the Nomination, People & Culture and Technology & Innovation Committees.

Background: Over 20 years' leadership experience as an academic physician/scientist across research, healthcare and medicine, and tertiary education. Former Dean, The University of Sydney's Sydney Medical School, Head of Medicine at Sydney's Royal North Shore Hospital and Head of the Cancer Genetics Laboratory at the Kolling Institute for Medical Research.

Other boards: Chairman, National Health and Medical Research Council. Director, MaynePharma and QBiotics. Director, Woolcock Institute of Medical Research and Senior Advisor to McKinsey & Company and MinterEllison.

Former directorships: Director of Firefly and Digital Health Agency CRC.

Qualifications: MD, MSc, FRACP, FAAHMS, FAICD

Abbas Hussain

Non-executive Director Age 55

Appointed to the Board 1 December 2018: Member of the Nomination, Medical Science and Technology & Innovation Committees.

Background: Over 30 years' global experience in the pharmaceutical industry with significant experience in building relationships with professionals within the healthcare industry. Former Global President, Pharmaceuticals at GlaxoSmithKline.

Other boards: Director, CSL Limited and Immunocore Limited. Senior Advisor, CellResearch Corp and C-Bridge Group, Hikma PLC, Director TARGTEX, Advisor to Indegene Inc.

Qualifications: BSc (Hons)

Michael Daniell

Non-executive Director Age 63

Appointed to the Board 1 January 2020: Member of the Nomination, Medical Science and Technology & Innovation Committees.

Background: Over 40 years' experience in the medical device industry with extensive executive leadership experience. Former Managing Director and CEO of Fisher & Paykel Healthcare Corporation Limited responsible for the global business and operations including the design, manufacture and marketing of innovative products and systems for use in respiratory care, acute care and treatment of obstructive sleep apnea.

Other boards: Director, Fisher & Paykel Healthcare Corporation Ltd, Council member, The University of Auckland, Director, Tait International Limited, Chair, New Zealand Medical Technology Centre of Research Excellence, Director, Medical Research Commercialisation Fund.

Qualifications: BE (Hons), Electrical, CMInstD (NZ)

Executive team

Dig Howitt

CEO & President

Dig joined Cochlear in 2000 and has a wealth of experience across the Company in roles including Chief Operating Officer, SVP, Manufacturing and Logistics and President, Asia Pacific. Prior to joining Cochlear, Dig worked for Boral and Boston Consulting Group. Dig is a member of the Male Champions of Change STEM group. He was appointed as President of Cochlear on 31 July 2017 and became CEO & President on 3 January 2018.

Qualifications: BE (Hons), MBA

Brent Cubis

Chief Financial Officer

Brent is responsible for accounting, corporate finance, treasury, audit, and investor relations. He joined Cochlear in February 2017 and has over 30 years' experience working in senior finance roles across a broad range of global industries and companies, including health, media (PBL Media) and property (Westfield, Bankers Trust and Sheraton). Brent qualified as a Chartered Accountant at Deloitte, which included a transfer to the US. Brent has also been a director for various charities and is an Alumni Leader for UNSW Business School.

Qualifications: BComm, CA

Jan Janssen

Chief Technology Officer

Jan leads a team of over 350 highly qualified engineers and scientists who implement the R&D strategy. This includes responsibility for identifying and developing cutting-edge technologies and bringing these innovations through to commercial products. Since 2017, he is also responsible for the business development strategy of Cochlear.

Jan started his career at Philips Electronics in 1990 and joined Cochlear in 2000 as Head of the Cochlear Technology Centre based in Belgium. After relocation to Sydney in 2003, Jan was promoted to SVP, Design and Development in 2005. In 2017, he was appointed Chief Technology Officer. Since 2019, Jan also has executive level accountability for quality and regulatory affairs.

Qualifications: MScEE

Tony Manna

President, Americas Region

Tony is responsible for the development and execution of the strategic direction for our North America operations.

Tony joined Cochlear in 2005 and has over 30 years' medical device experience, including senior commercial management roles at BEI Medical and Gyrus Medical. Prior roles in Cochlear include VP, Sales USA, General Manager, Cochlear Bone Anchored Solutions, USA and President, Cochlear Bone Anchored Solutions, Sweden.

Qualifications: BS EET

Richard Brook

President, EMEA & Latin American Region

Richard is responsible for the development and execution of the strategic direction for all our operations in Europe, Middle East and Africa (EMEA) and Latin America. This includes sales in over 60 countries.

Before joining Cochlear in 2003, Richard held senior roles in Guidant Corporation and Alaris Medical Systems. He has over 30 years' experience in the medical device industry.

Qualifications: BSc Management, MBA

Anthony Bishop

President, Asia Pacific Region

Anthony was appointed President, Asia Pacific in July 2016. Anthony is responsible for the development and execution of the strategic direction for all our operations in Australia, Asia and the South Pacific.

Anthony joined Cochlear in July 2015 as Director of Marketing and Business Development, Asia Pacific. Prior to Cochlear, Anthony spent 21 years at Johnson & Johnson Medical in various roles including marketing, sales and general management around the world including being Managing Director, Johnson & Johnson Medical, Australia/New Zealand prior to joining Cochlear.

Qualifications: BBus (Hons), MManagement, GAICD

Rom Mendel

President, Acoustics

Rom is responsible for the development and execution of the strategic direction for our Acoustics business and is the General Manager for Cochlear Bone Anchored Solutions, Sweden.

Rom joined Cochlear in 2007. He has over 20 years' experience in various commercial roles within hearing care and other high-tech industries in Denmark, the US and Sweden including senior commercial management roles at Oticon and Eicon Networks. Prior roles in Cochlear include Director of Marketing Cochlear Bone Anchored Solutions, Sweden and General Manager, Cochlear Bone Anchored Solutions, USA.

Qualifications: MSc International Business, BSc

Stu Sayers

President, Services

Stu was appointed as Cochlear's inaugural President, Services in May 2016. The Services business provides aftercare services for Cochlear recipients and professionals, generating revenue from post-implant products and other offerings.

Stu comes with a wealth of experience in establishing and building customer-focused business-to-customer and business-to-business service businesses, online and at scale. Most recently, Stu led the Amazon subsidiary Audible in Asia Pacific. Prior to Amazon, Stu ran E*TRADE and then Yahoo!7 in Australia and New Zealand. Prior to that, he worked for Procter & Gamble and McKinsey & Company.

Qualifications: BEc (Hons), MBA

Dean Phizacklea

Senior Vice President, Global Marketing

Dean joined Cochlear in June 2016. Dean has responsibility for product marketing and commercialisation, consumer marketing, innovation, market access, market insights and corporate communications.

Dean has more than 20 years' experience in medical devices and pharmaceuticals, covering a range of senior commercial roles in the US, Japan, Europe and Australia. Prior to joining Cochlear, Dean led Global Strategic Marketing for Abbott Diabetes Care. Other roles include General Manager for Abbott's pharmaceutical and diabetes care businesses in Australia/New Zealand and commercial roles in Asia with AstraZeneca.

Qualifications: BSc Microbiology, MBA

David Hackshall

Chief Information Officer

David joined Cochlear in July 2015 as Cochlear's first Chief Information Officer and has global responsibility for the Company's information technology strategy and management. David's focus is to ensure Cochlear has the platforms in place to deliver and drive growth. This capability is critical in connecting Cochlear with both professionals and recipients and evolving Cochlear into both a business-to-business as well as business-to-customer organisation.

Prior to Cochlear, David was Chief Information Officer at Wesfarmers Insurance Ltd and brings over 15 years of executive experience across the communications, logistics and finance sectors.

Qualifications: DipFN, MIT, MBA

Greg Bodkin

Senior Vice President, Supply Chain & Operational Excellence

Greg has functional responsibility for new product industrialisation, procurement, manufacturing, logistics and warranty & repair. These functions enable the technologies developed in design and development to be supplied as commercial products in Cochlear's global markets. In addition, he leads the Cochlear Program Office and management of the Global Property portfolio.

Greg joined Cochlear in 2007 as Head of Supply with 20 years' prior experience in supply chain management and operations consulting positions, including appointments at Taylor Ceramic Engineering, Warman International Ltd, Weir Minerals PLC and National Australia Bank. In August 2014, he was promoted to the position of SVP Manufacturing and Logistics. In January 2018, he was promoted to the position of SVP, Supply Chain & Operational Excellence.

Qualifications: BE (Hons), MComm (UNSW)

Jennifer Hornery

Senior Vice President, People & Culture

Jennifer joined Cochlear in 2008 as Senior HR Business Partner with responsibility for manufacturing and logistics and safety and wellness before taking on responsibility for People & Culture Business Partnering for Cochlear's global functions in 2016. Jennifer was appointed SVP, People & Culture in 2017 and her focus is to ensure the right strategic capabilities, organisation and culture are in place to support Cochlear's performance and growth aspirations.

Prior to Cochlear, Jennifer worked in commercial, strategy and HR leadership roles across a number of industries within Australia and the US, including senior positions at Campbell Arnott's and Booz & Company.

Qualifications: BComm, MBA, GAICD

Brian Kaplan

Senior Vice President, Clinical Strategy and Innovation

Brian joined Cochlear in 2016 and manages clinical strategy and innovation for Cochlear. He is responsible for the clinical data to support present and future products and services. Brian dedicates two-thirds of his time to his role at Cochlear, while continuing to direct a cochlear implant surgical practice at the Greater Baltimore Medical Center.

Brian's past research interests have included hearing loss, balance disorders, and hair cell regeneration. His current practice focuses on adult and paediatric otology, with an emphasis on hearing restoration. Brian is board-certified in otolaryngology and is a Fellow of the American College of Surgeons.

Brian has completed an Otolaryngology residency at the University of Virginia, is the Chairman, Department of Otolaryngology at the Greater Baltimore Medical Center and Director, Presbyterian Board of Governors Cochlear Implant Center at the Greater Baltimore Medical Center.

Qualifications: BNeuroSci, BA, MD, FACS

Remuneration report

Letter from the Chair of the People & Culture Committee (P&CC)

Dear Shareholders

On behalf of the Cochlear Board, I present to you the FY20 Remuneration report where we outline Cochlear's remuneration strategy, summarise the performance outcomes for FY20 and detail the associated remuneration outcomes for Cochlear's key management personnel.

Cochlear had a strong start to FY20. From mid-March, however, the impact on profitability from an adverse litigation judgment and COVID-19 was significant. During this period of uncertainty, the Board and management made every effort to retain its highly skilled workforce and investment in research and development programs. The Board undertook several measures to help share the burden with shareholders and protect the long-term future of the Company including:

- Reductions in Board and executive pay for a period of three months commencing mid-April 2020:
    - Non-executive directors took a 30% reduction in Board and committee fees;
    - The CEO & President (CEO&P) took a 30% reduction in base salary; and
    - Other executives took a 20% reduction in base salary;
- No short-term incentive (STI) for FY20 was paid; and
- No fixed pay increases for the Board or executive team were made for FY21.

FY20 performance and reward outcomes

The Board is satisfied that the reward outcomes under the STI and long-term incentive (LTI) plans for FY20 reflect the Company's performance in this challenging period.

The Board made changes to the STI plan in FY20 by introducing a minimum net profit after tax (NPAT) gateway, in addition to revenue growth targets and achievement of Company strategic objectives. Due to the significant impact that COVID-19 had on the business, NPAT guidance was withdrawn in March 2020 and the NPAT gateway on the STI plan was not achieved. The Board considered a range of additional factors, including the disruption of COVID-19 and the impact of the patent litigation decision, and determined that no discretion would be applied to the FY20 STI plan, resulting in no STI payments made to any employee, including executives.

For LTI, Cochlear's performance hurdles of relative total shareholder return against the ASX 100 was at the 72nd percentile and basic earnings per share (EPS) represented a (12.9%) compound annual growth rate over the last three years. Based on these results, 46.4% of the FY18-20 LTI vested to the CEO&P and executives. There was no vesting for the EPS portion of the FY18-20 LTI plan. Further detail on this year's remuneration outcomes are provided in this report.

Our executive remuneration framework

The Board is committed to ensure our executive remuneration framework and the associated reward outcomes align with our business objectives, performance and shareholder expectations.

After extensive consultation, the Board introduced changes to the LTI plan for FY20, including extending the performance period from three to four years and recalibrating target and maximum EPS measures to align to the Company's growth targets and current market conditions.

As mentioned in the Letter to shareholders, due to the uncertain timing of a global recovery from the pandemic, we cannot accurately forecast the future impact this will have on our operations and financial results over the next 12 months. For this reason, the Board anticipates that discretion will need to be considered and applied (upwards or downwards) using the parameters of our existing remuneration framework at the end of the FY21 performance period. This will ensure fair and equitable remuneration outcomes for executives that enable Cochlear to continue to engage and retain our highly skilled workforce, and consider a range of stakeholders including shareholders, customers and the community.

The Board believes Cochlear's approach to Board and executive remuneration remains balanced, fair and equitable, and rewards and motivates a successful and experienced executive team to ensure Cochlear is successful over the long term.

Glen Boreham, AM
Chair, People & Culture Committee

Contents

This report covers:

The information provided in this Remuneration report (except for section 2 and section 8.3) has been audited as required by section 308(3C) of the *Corporations Act 2001*.

1. Key management personnel

This report covers key management personnel (KMP) who have authority for planning, directing and controlling the activities of Cochlear and comprise non-executive directors (NEDs) and executive KMP as outlined in the table below.

Name	Position	Term as KMP
Non-executive directors		
Rick Holliday-Smith	Chairman	Full year
Yasmin Allen	Non-executive director	Full year
Glen Boreham, AM	Non-executive director	Full year
Michael Daniell	Non-executive director	Part year - appointed 1 January 2020
Alison Deans	Non-executive director	Full year
Andrew Denver	Non-executive director	Full year
Abbas Hussain	Non-executive director	Full year
Donal O'Dwyer	Non-executive director	Full year
Bruce Robinson, AC	Non-executive director	Full year
Executive KMP		
Dig Howitt	CEO & President (CEO&P)	Full year
Anthony Bishop	President, Asia Pacific Region	Full year
Richard Brook	President, EMEA & Latin American Region	Full year
Brent Cubis	Chief Financial Officer	Full year
Jan Janssen	Chief Technology Officer	Full year
Tony Manna	President, Americas Region	Full year

As announced to the market on 13 July 2020, Brent Cubis, Chief Financial Officer, will be leaving Cochlear at the end of calendar year 2020.

2. Executive KMP remuneration received in FY20 (unaudited)

The table below presents the remuneration paid to, received by or vested to each executive KMP during the year. Fixed remuneration and cash STI relate to amounts earned during the year and vested deferred STI and vested LTI represent equity vesting from prior years.

The figures presented below are different to the statutory disclosures in section 5 which are prepared in accordance with the accounting standards and therefore include the accounting value for all unvested deferred STI and LTI awards expensed in the year. The table below has been provided voluntarily to ensure shareholders are able to clearly understand the remuneration outcomes and actual 'take-home pay' of executive KMP for FY20.

Amounts $	Year	Fixed remuneration[1]	Cash STI[2]	Vested deferred STI[3]	Vested LTI[4]	Total
Executive KMP						
Dig Howitt	**FY20**	**1,744,153**	**-**	**206,683**	**864,687**	**2,815,523**
	FY19	1,725,969	1,105,225	155,430	2,075,203	5,061,827
Anthony Bishop	**FY20**	**561,171**	**-**	**129,803**	**272,124**	**963,097**
	FY19	524,528	244,481	148,896	-	917,905
Richard Brook	**FY20**	**1,045,039**	**-**	**205,594**	**682,358**	**1,932,991**
	FY19	1,009,004	360,020	164,934	1,858,388	3,392,347
Brent Cubis	**FY20**	**633,651**	**-**	**52,923**	**-**	**686,574**
	FY19	633,522	284,927	-	-	918,449
Jan Janssen	**FY20**	**851,002**	**-**	**188,824**	**706,925**	**1,746,751**
	FY19	783,783	422,605	153,450	1,436,076	2,795,914
Tony Manna	**FY20**	**923,513**	**-**	**216,701**	**686,174**	**1,826,388**
	FY19	850,835	353,068	147,114	1,293,946	2,644,963

1. Fixed remuneration earned in the year (base salary, superannuation and non-monetary benefits which may include insurances and car allowances). Richard Brook's fixed remuneration for FY20 and FY19 excludes employer contributions for social security, accident and sickness and reflects actual 'take-home pay'. These amounts are presented in the statutory table in section 5. Tony Manna's non-monetary benefits for the FY19 comparative year have been adjusted from $75,508 to $87,762, with the total for FY19 adjusted accordingly.
2. Cash STI earned and relating to performance during the financial year. For example, FY20 is reported as STI payments which are accrued at year end, and received in August 2020, after the reporting year end.
3. Vested deferred STI is the value of the deferred STI from prior years that vested in August of the reported financial year (calculated as the number of rights that vested multiplied by the share price on the vesting date). For example, FY20 is reported as the FY17 deferred STI grant which vested in August 2019.
4. Vested LTI is the value of performance rights and options that vested in August of the reported financial year (rights are calculated as the number of rights that vested multiplied by the share price on the vesting date and options are calculated as the number of options multiplied by the share price on the date of vesting/exercise less the exercise price). For example, FY20 is reported as the FY17 LTI grant which vested in August 2019 (79.3% of awards vested due to performance).

3. Our remuneration strategy and framework

Cochlear's executive remuneration strategy is designed to attract, motivate and retain a highly qualified and experienced group of executives employed across diverse geographies. The following diagram links each of the executive team remuneration components to Cochlear's mission and strategy.

Cochlear's mission and strategy

To help people hear and be heard

We deliver this through our corporate strategy…

Retain market leadership

Grow the hearing implant market

Deliver consistent revenue and earnings growth

and four strategic platforms…

Grow the core

Build a Service business

Shape the organisation

Value creation

which are reflected in performance measures across Cochlear's incentive plans…

Net profit after tax (NPAT)
Sales revenue

Achievement of business priorities and growth initiatives

Relative total shareholder return (TSR)

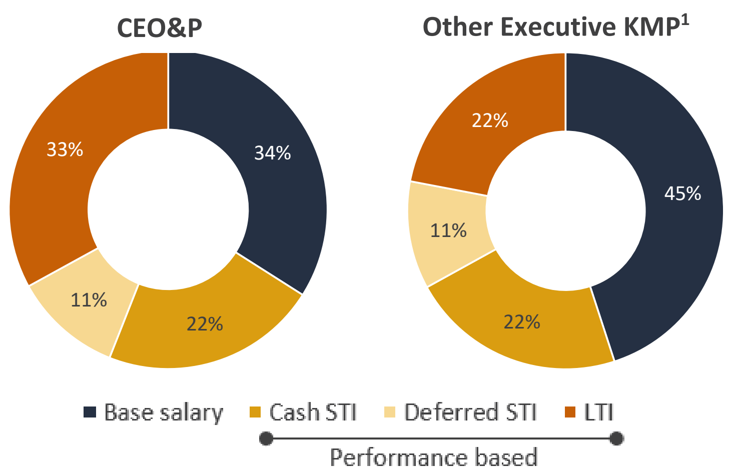
Compound annual growth rate in earnings per share (EPS)

with actual outcomes directly driving executive remuneration.

Fixed remuneration + Short-term incentive + Long-term incentive = Total remuneration

3.1 Target remuneration mix

The remuneration mix for executive KMP is weighted towards at-risk performance based remuneration to ensure a strong focus on short, medium and long-term performance. A portion of executive remuneration is paid in equity (44% for the CEO&P and 33% for other executive KMP) to align our executives with shareholder interests.



[1] Excludes the transitional arrangement for FY20 where executives (excluding the CEO&P) had an LTI opportunity of 62.5% of base salary. Refer to section 3.4 for more detail.

3.2 Fixed remuneration

Fixed remuneration comprises base salary, superannuation and non-monetary benefits which may include insurances and car allowances. It is set at a level to attract and retain executive talent with the appropriate capabilities to deliver Cochlear's objectives.

Fixed remuneration is generally positioned at the median of the relevant market and is reviewed annually to ensure alignment with local market benchmarks, and it is reflective of the executive's expertise and performance in the role. Market benchmarks are typically set with reference to market capitalisation and include organisations within Cochlear's industry sector and/or similar in global operations and complexity as determined by the P&CC each year.

3.3 Short-term incentive

<table>
<tr><td>Purpose</td><td>To align and reward executives for the achievement of Cochlear group and regional (for regional executives) performance targets set by the Board at the beginning of the performance period.</td></tr>
<tr><td>Performance measures</td><td>STI is dependent on meeting financial and strategic performance measures:
<table>
<tr><th>Performance measure and weighting</th><th>Description</th></tr>
<tr><td>Performance Gateway</td><td>• Group Performance Gateway (minimum NPAT threshold) to drive global alignment.</td></tr>
<tr><td>Sales revenue (60%)</td><td>• Sales revenue growth is critical to short and longer-term shareholder returns.
• Financial targets are set by the Board, having regard to prior year performance, global market conditions, competitive environment, future prospects and Board approved budgets. The targets incorporate a significant amount of stretch to ensure executives are engaged and incentivised to appropriately deliver results. The specific targets are not disclosed to the market due to their commercial sensitivity.
• The weighting between Cochlear group and regional financial targets depends on the responsibilities and scope of influence of the executive.</td></tr>
<tr><td>Strategic measures (40%)</td><td>• Strategic measures recognise that in addition to short-term financial results, a number of strategic initiatives are required to enable sustained growth over time.</td></tr>
<tr><td>Individual contribution</td><td>• Each executive's contribution against performance objectives is assessed at an individual level at the end of the performance period. This assessment determines the level at which awards are made.</td></tr>
</table>
Validation of performance against the measures set for:
• the CEO&P involves a review by the Board based on financial inputs from the Chief Financial Officer, and approved by the P&CC and Board each year; and
• other executive KMP involves a review by the CEO&P based on inputs from the Chief Financial Officer and approved by the P&CC.
Any anomalies or discretionary elements are validated and approved by the Board.
Refer to section 4 for further detail on measures for FY20.</td></tr>
<tr><td>Opportunity</td><td>CEO&P: target opportunity is 100% of base salary, and maximum is up to 180% of base salary.
Other executive KMP: target opportunity is 75% of base salary, and maximum is up to 135% of base salary.</td></tr>
<tr><td>Delivery</td><td>Two-thirds of the award is paid in cash annually, with one-third deferred into service rights for a period of two years (subject to a service condition) to reinforce alignment to longer-term shareholder interests and for retention purposes. No dividends are attached to service rights.
The number of rights to be allocated is calculated using the 'gross contract value', which refers to a Black-Scholes-Merton pricing model without discounting for service or performance hurdles. The model uses Cochlear's share price following the announcement of full year results in August each year.</td></tr>
<tr><td>Cessation of employment</td><td>Prior to STI payment date: if an executive ceases employment with Cochlear prior to any cash being paid, or service rights being granted, the executive will forfeit any awards to be paid for the performance period, unless the Board determines otherwise.
Post STI payment date: if an executive is dismissed for serious misconduct or resigns from their position after service rights have been granted, but prior to the relevant vesting date, any unvested rights will generally be forfeited, unless the Board determines otherwise.</td></tr>
</table>

3.4 Long-term incentive

Purpose	To align the remuneration opportunity for the executive team with shareholder value and provide a stimulus for the retention of executives within the Company.
Award vehicle	LTI is delivered as 50% options and 50% performance rights.
Opportunity	**CEO&P:** maximum opportunity is 100% of base salary. **Other executive KMP:** maximum opportunity is 50% of base salary. For FY20, a transitional arrangement was implemented to recognise that increasing the performance period from three to four years will result in a gap year of LTI vesting in FY22 for executives. In FY20, executives (excluding the CEO&P) had an opportunity of 62.5% of base salary.
Allocation method	The LTI opportunity is calculated using the ‘gross contract value’, which refers to a Black-Scholes-Merton pricing model without discounting for service or performance hurdles. Gross contract value discounts for dividends not paid, share price volatility and the risk free rate of return. There is no discount for the likelihood of service or performance conditions. The model uses Cochlear’s five-day volume-weighted average share price following the announcement of full year results in August each year.
Performance period	Performance is measured over a four-year performance period. Post vesting, options expire seven months after the vesting date if they have not been exercised. There is no retesting of performance hurdles under the LTI plan. For FY20, a transitional arrangement was implemented to recognise that increasing the performance period from three to four years will result in a gap year of LTI vesting in FY22 for executives. For FY20 only, two grants were provided to the executive team (excluding the CEO&P): • grant 1: 50% of the annual LTI grant opportunity with a three-year performance period; and • grant 2: 75% of the annual LTI grant opportunity with a four-year performance period. No transitional arrangement was provided to the CEO&P. The CEO&P’s FY20 LTI grant opportunity continued to be 100% of base salary with a four-year performance period.
Performance measures and hurdles	Awards are subject to: • 50% weighting on relative TSR against the constituents of the ASX 100 index as at the start of the performance period; and • 50% weighting on compound annual growth rate (CAGR) in EPS. The proportion of awards that vest for performance are:

Relative TSR	
Performance	**% of instruments that vest**
Less than 50^{th} percentile	0%
At the 50^{th} percentile	40%
50^{th} percentile to 75^{th} percentile	40% to 100% (pro-rata)
Above 75^{th} percentile	100%

EPS	
Performance (CAGR)	**% of instruments that vest**
Less than 7.5%	0%
7.5%	50%
7.5% to 12.5%	50% to 100% (pro-rata)
Above 12.5%	100%

These measures have been selected to incentivise the executive team towards long-term sustainable growth of the business and are generally accepted proxies for the creation of shareholder value.

Dividends	No dividends are attached to options or performance rights.
Cessation of employment	If an executive ceases employment with Cochlear before the end of the performance period, unvested LTI awards will generally be forfeited. In exceptional circumstances (including, but not limited to, redundancy and retirement), the Board may in its discretion, determine that all or a portion of the award will vest in line with the original performance criteria and vesting date.

4. Executive KMP remuneration and link to performance

4.1 FY20 STI outcomes

STI is based on meeting a Group Performance Gateway of NPAT, and performance against financial measures (60%) and strategic measures (40%).

In FY20, Cochlear experienced a significant and rapid decline in revenue from mid-March to early May, as a result of COVID-19 with elective surgeries deferred across the world. As a result, the Group Performance Gateway was not met, and no STI pool was created for FY20.

Under the terms of the plan, the Board is able to exercise discretion to create or modify (upwards or downwards) the award pool to allow payments to be made. After a holistic assessment of business performance, and consideration of shareholder experience during this period, the Board decided to not exercise discretion and no STI awards (including deferred STI grants) were made to any employee (including executives) under the plan.

The table below provides a summary, and achievement against each, of the financial and strategic measures of the STI plan. Measures were agreed with the P&CC at the commencement of the financial year and aligned to the delivery of initiatives that support Cochlear's strategic priorities.

	Strategic priority	Business priority	Commentary on performance	Achievement
Strategic measures (40%)	Retain market leadership	• Launch new products and services • Drive upgrade penetration • Ensure technology leadership • Develop organisational talent and capability • Implement the digital strategy • Develop partnerships and alliances • Drive One Cochlear and operational excellence • Increase recipient engagement • Create world-class customer experiences	• Strengthened product portfolio for Cochlear Implants and Acoustics with launch of new acoustic and cochlear implants • Extended leadership in connected services with Remote Check launch • Increased organisational capability through investment in leadership development and sales presence • Implemented initiatives to improve customer experience, including expanding Cochlear Family membership • Continued efficiency gains in supply chain, customer service and procurement	
	Grow the hearing implant market	• Increase access and funding • Expand and enhance direct-to-consumer capability • Build referrals from the Hearing Aid and ENT channel	• Strengthened direct-to-consumer capability in existing markets, and launched in more countries • Implemented market access initiatives • Expanded growth programs to build the referral channel	
Financial measures (60%)	Deliver consistent revenue and earnings growth	• Achieve the FY20 financial targets	• Financial targets were not met due to the impact of COVID-19 on sales revenue, combined with the cost of an adverse litigation judgment • Raised capital and increased debt facilities to strengthen balance sheet and liquidity position • Implemented a significant reduction in non-essential spending and capital expenditure	

= Below expectations = Met expectations = Exceeded expectations

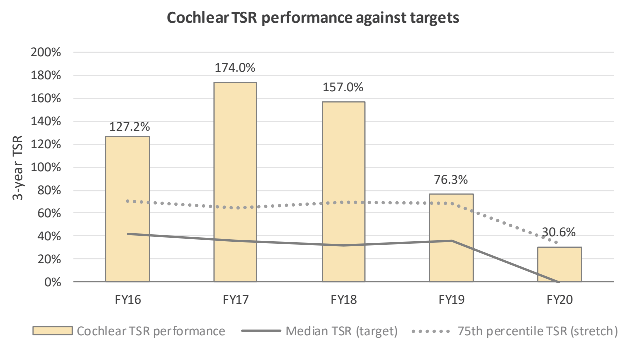
As a result of performance, no FY20 STI payments were made as outlined in the table below.

Executive KMP	STI target as a % of base salary	STI maximum as a % of base salary	Actual STI as a % of target	Actual STI as a % of maximum	STI forfeited as a % of maximum	Actual STI ($)
Dig Howitt	100%	180%	0%	0%	100%	0
Anthony Bishop	75%	135%	0%	0%	100%	0
Richard Brook	75%	135%	0%	0%	100%	0
Brent Cubis	75%	135%	0%	0%	100%	0
Jan Janssen	75%	135%	0%	0%	100%	0
Tony Manna	75%	135%	0%	0%	100%	0

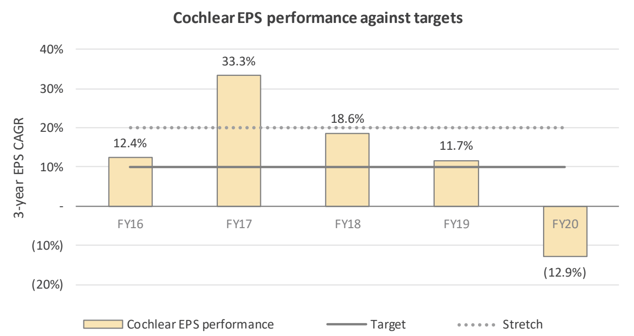
4.2 FY18-20 LTI vesting outcomes

LTI is based on performance against relative TSR (50%) and EPS growth (50%) over a three-year performance period. The graphs below illustrate Cochlear's relative TSR and EPS performance over the past five years.

For FY20, Cochlear's TSR performance was 30.6%, which was ranked at the 72nd percentile of the ASX 100 comparator group. This resulted in performance between target and stretch, and as a result, 92.8% of the TSR portion of the LTI vested.



Cochlear's underlying EPS[1] in FY20 was 257.9 cents, which is a (12.9%) CAGR over the three-year performance period. This resulted in performance below target and as a result, 0% of the EPS portion of the LTI vested.



For the FY18-20 LTI, 46.4% vests based on performance over the three-year period from 1 July 2017 to 30 June 2020.

1. Underlying EPS excludes innovation fund gains and patent litigation expense.

4.3 Financial performance history (FY16 to FY20)

	FY16	FY17	FY18	FY19	FY20
Sales revenue ($million)[1]	1,158.1	1,239.7	1,351.4	1,446.1	1,352.3
Earnings/(loss) before interest and tax (EBIT) ($million)	262.6	315.6	348.4	370.1	(262.2)
EBIT (excluding innovation fund gains and patent litigation expense) ($million)	n/a	n/a	350.6	359.3	206.9
Net profit/(loss) after tax (NPAT) ($million)	188.9	223.6	245.8	276.7	(238.3)
NPAT (excluding innovation fund gains and patent litigation expense) ($million)	n/a	n/a	248.0	265.9	153.8
Basic earnings/(loss) per share (EPS) (cents) – reported	330.6	389.7	427.3	479.6	(399.6)
Basic EPS (excluding innovation fund gains and patent litigation expense) (cents)	n/a	n/a	431.1	460.9	257.9
EPS growth (3-year CAGR)	12.4%	33.3%	18.6%	13.2%	(200.8%)
EPS growth (excluding innovation fund gains and patent litigation expense) (3-year CAGR)	n/a	n/a	n/a	11.7%	(12.9%)
Total dividend per share ($)[2]	2.30	2.70	3.00	3.30	1.60
Share price as at 30 June ($)	121.25	155.45	200.17	206.84	188.93
Relative total shareholder return (TSR) (3 years)	127.2%	174.0%	157.0%	76.3%	30.6%
TSR percentile ranking[3]	94th	96th	97th	81st	72nd

1. Excludes foreign exchange gain/(loss) on hedged sales.
2. No final FY20 dividend; $1.60 is the interim dividend for FY20.
3. TSR percentile ranking is shown over three financial years to 30 June. For LTI, performance is compared to the TSR of the constituents of the ASX 100 as at the start of the relevant performance period.

For further explanation of details on Cochlear performance, see the Operating and financial review section on pages 15 to 32 of this Annual Report.

5. Executive KMP statutory remuneration disclosure

The table below presents the total remuneration for executive KMP in accordance with the accounting standards.

Amounts $	Year	Short-term benefits			Post-employment	Other long-term benefits	Share based payments			Total	% of performance related remuneration
		Salary	Cash STI	Non-monetary benefits[1]	Super-annuation contributions	Long service leave	Deferred STI[2]	LTI performance rights[3]	LTI options[3]		
Executive KMP											
Dig Howitt	**FY20**	**1,721,612**	**-**	**1,538**	**21,003**	**41,051**	**298,081**	**151,890**	**463,205**	**2,698,380**	**33.84%**
	FY19	1,704,308	1,105,225	1,130	20,531	(19,078)	344,269	124,402	413,778	3,694,565	53.80%
Anthony Bishop	**FY20**	**539,245**	**-**	**923**	**21,003**	**6,549**	**70,316**	**38,756**	**36,625**	**713,417**	**20.42%**
	FY19	503,356	244,481	640	20,531	2,583	99,369	45,172	24,710	940,842	43.97%
Richard Brook	**FY20**	**767,993**	**-**	**235,341**	**152,924**	**-**	**104,762**	**53,498**	**79,027**	**1,393,545**	**17.03%**
	FY19	753,728	360,020	275,439	152,836	-	150,706	89,567	75,067	1,857,363	36.36%
Brent Cubis	**FY20**	**611,725**	**-**	**923**	**21,003**	**4,397**	**84,302**	**52,062**	**59,666**	**834,078**	**23.50%**
	FY19	612,350	284,927	640	20,531	2,472	96,139	34,503	35,415	1,086,977	41.49%
Jan Janssen	**FY20**	**828,461**	**-**	**1,538**	**21,003**	**4,869**	**115,315**	**60,412**	**88,868**	**1,120,466**	**23.61%**
	FY19	762,121	422,605	1,130	20,531	22,880	157,525	69,669	88,896	1,545,357	47.80%
Tony Manna	**FY20**	**816,517**	**-**	**85,755**	**21,241**	**-**	**102,227**	**36,386**	**111,795**	**1,173,921**	**21.33%**
	FY19	743,718	353,068	87,762	19,355	-	150,682	30,346	120,337	1,505,268	43.48%
Total	**FY20**	**5,285,553**	**-**	**326,018**	**258,177**	**56,866**	**775,003**	**393,004**	**839,186**	**7,933,807**	**25.30%**
	FY19	5,079,581	2,770,326	366,741	254,315	8,857	998,690	393,659	758,203	10,630,372	46.29%

1. Non-monetary benefits include insurances for all KMP and car and housing allowances for overseas based KMP which are market-based payments. For Richard Brook, the amount also includes compulsory social security contributions of approximately $111,000. Tony Manna's non-monetary benefits for the FY19 comparative year have been adjusted from $75,508 to $87,762, with the totals for FY19 adjusted accordingly.
2. Deferred STI is granted in service rights and deferred for a further two years. The cost of the plan is expensed across three years. The FY20 amount represents the portion of the FY18 and FY19 deferred STI expensed in FY20. The FY19 amount represents the portion of the FY17, FY18 and FY19 deferred STI expensed in FY19.
3. LTI granted in performance rights and options are expensed evenly over the period from grant date to vesting date. The value is calculated at the date of grant using the Black-Scholes-Merton pricing model discounted for vesting probabilities of non-market performance criteria. The amount expensed each reporting period includes adjustments to the life-to-date expense of grants based on the reassessed estimate of achieving non-market performance criteria and final vesting amounts for the non-market performance criteria of performance rights and options. The value disclosed above is the portion of the value of the performance rights and options recognised as an expense in the financial year. The ability to exercise the performance rights and options is conditional on Cochlear achieving certain performance hurdles. Further details of performance rights and options granted during the financial year are set out in this report.

6. Executive service agreements

Cochlear does not enter into (limited) service contracts for executive KMP. The terms of employment for executive KMP meet local employment law requirements. Key provisions are similar but do, on occasion, vary to suit different needs.

The following sets out details of the employment agreements relating to executive KMP.

Length of contract	Permanent contract until notice is given by either party.
Notice periods	CEO&P: 12 months' written notice by either party. Other executive KMP: between 60 days to six months' written notice by either party (exact period specified in each contract).
Post-employment restraints	All executive KMP are subject to post-employment restraints for up to 12 months.
Other arrangements	Richard Brook will receive a maximum of CHF 30,000 for repatriation costs in the case of termination or resignation.

7. Remuneration governance

7.1 Governance framework for remuneration at Cochlear

The Board is responsible for all areas of Cochlear's strategy and policy related to its people. Consistent with this responsibility, the Board has established the P&CC which comprises solely of independent NEDs.

Management

- Makes recommendations to the P&CC with respect to individual remuneration arrangements for executive KMP
- Implement policies and practices relating to talent management, remuneration, organisational culture, diversity and inclusion, work, health and safety and leadership development

People & Culture Committee

- The P&CC is empowered to source any internal resources and obtain external independent professional advice it considers necessary to enable it to review management proposals and make decisions on behalf of the Board on:
  - Remuneration policy, composition, quantum and performance targets for executive KMP
  - Remuneration policy in respect of NEDs
  - Organisational culture, diversity and inclusion, talent management and leadership development strategies and practices
  - Work, health and safety metrics and initiatives
  - Design features of employee and executive short-term and long-term incentive plan awards

Board

- Reviews, applies judgment and, as appropriate, approves recommendations from the P&CC

7.2 Advice from external advisors

To inform decisions, the P&CC sought advice and, at times, recommendations from the CEO&P and other management throughout the year.

During FY20, the P&CC engaged Godfrey Remuneration Group (GRG) and received market practice advice and information in relation to the remuneration of NEDs, executives and senior leaders. GRG was paid $57,100 (excluding GST) for these services.

The P&CC is satisfied that the advice received from GRG is free from undue influence of the KMP to whom the remuneration recommendations relate as GRG confirmed in writing that the remuneration recommendations were made free from undue influence by management, in accordance with the *Corporations Act 2001*.

7.3 Share ownership requirements

Executive KMP are required to retain vested equity until they hold and maintain a holding of Cochlear shares equivalent to their annual salary in the previous year. The Board considers the minimum shareholding guidelines to be best practice to strengthen the alignment of executives' interests to those of shareholders. The table in section 8.2 details the current holdings of executive KMP.

7.4 Clawback Policy and discretion

All participants of the deferred STI and LTI plans are subject to the Clawback Policy, available in the 'Investor Centre' section of the Company's website. The policy enables the Board to claw back remuneration outcomes in the event of a material non-compliance with any financial reporting requirement, misconduct, or following inappropriate behaviour post-employment in cases where the Board has exercised its discretion to allow retention of equity following termination of employment. The policy is designed to further align the interests of participants with the long-term interests of Cochlear and shareholders, and to ensure that excessive risk taking is not rewarded.

The Board retains discretion to adjust remuneration outcomes upwards or downwards to ensure incentives are not provided where it would be inappropriate or would provide unintended outcomes. The exercise of appropriate discretion may be used where a formulaic outcome does not align with the overall shareholder experience, or reflect overall business performance and intended outcomes, or leads to retention risk for key talent. The Board balances judgment on remuneration outcomes with consideration to all stakeholders.

8. Executive KMP equity disclosures

Executive KMP participate in the deferred STI and LTI plan which offers equity under the Cochlear Executive Incentive Plan (CEIP). The purpose of the CEIP is to encourage executives to hold Cochlear shares and to align their interests to shareholders' interests.

Under the LTI plan, vesting of options or performance rights only occurs if Cochlear achieves challenging and market competitive hurdles related to EPS growth and relative TSR. Under the deferred STI plan, grants are based on performance in the first year, and are then deferred for a further two years.

8.1 Equity granted as remuneration

The table below presents the number of options and performance rights granted to executive KMP as well as the number of instruments that vested or were forfeited during the year.

No options or rights vest if the conditions are not satisfied, hence the minimum value is nil. The maximum value of the grants has been determined as the fair value of awards at grant date that is yet to be expensed.

Executive KMP	Plan	Grant date	Options		Performance rights		Vesting date	Vested	Forfeited
			Number	Maximum value to be expensed ($)[1]	Number	Maximum value to be expensed ($)[1]			
Dig Howitt	FY17 LTI	19-Oct-16	10,375	-	1,537	-	19-Aug-19	79.3%	20.7%
	FY17 deferred STI	24-Aug-17	-	-	949	-	19-Aug-19	100.0%	0.0%
	FY18 LTI	18-Oct-17	46,842	-	3,372	-	19-Aug-20		
	FY18 deferred STI	24-Aug-18	-	-	1,692	-	19-Aug-20		
	FY19 LTI	17-Oct-18	35,907	194,795	1,685	32,719	18-Aug-21		
	FY19 deferred STI	17-Sep-19	-	-	2,634	184,161	18-Aug-21		
	FY20 LTI	23-Oct-19	24,041	322,228	4,432	221,054	16-Aug-23		
	Total		**117,165**	**517,023**	**16,301**	**437,934**			
Anthony Bishop	FY17 LTI	19-Oct-16	2,171	-	751	-	19-Aug-19	79.3%	20.7%
	FY17 deferred STI	24-Aug-17	-	-	596	-	19-Aug-19	100.0%	0.0%
	FY18 LTI	18-Oct-17	1,778	-	697	-	19-Aug-20		
	FY18 deferred STI	24-Aug-18	-	-	440	-	19-Aug-20		
	FY19 LTI	17-Oct-18	1,598	8,669	700	13,592	18-Aug-21		
	FY19 deferred STI	17-Sep-19	-	-	582	40,692	18-Aug-21		
	FY20 LTI	23-Oct-19	2,014	21,121	332	14,439	17-Aug-22		
	FY20 LTI	23-Oct-19	2,745	36,792	506	25,238	16-Aug-23		
	Total		**10,306**	**66,582**	**4,604**	**93,961**			

Executive KMP	Plan	Grant date	Options		Performance rights		Vesting date	Vested	Forfeited
			Number	Maximum value to be expensed ($)[1]	Number	Maximum value to be expensed ($)[1]			
Richard Brook	FY17 LTI	19-Oct-16	5,622	-	1,944	-	19-Aug-19	79.3%	20.7%
	FY17 deferred STI	24-Aug-17	-	-	944	-	19-Aug-19	100.0%	0.0%
	FY18 LTI	18-Oct-17	6,965	-	1,170	-	19-Aug-20		
	FY18 deferred STI	24-Aug-18	-	-	665	-	19-Aug-20		
	FY19 LTI	17-Oct-18	4,565	24,765	857	16,641	18-Aug-21		
	FY19 deferred STI	17-Sep-19	-	-	858	59,989	18-Aug-21		
	FY20 LTI	23-Oct-19	2,679	28,096	442	19,223	17-Aug-22		
	FY20 LTI	23-Oct-19	3,652	48,949	673	33,567	16-Aug-23		
	Total		**23,483**	**101,810**	**7,553**	**129,420**			
Brent Cubis	FY17 deferred STI	24-Aug-17	-	-	243	-	19-Aug-19	100.0%	0.0%
	FY18 LTI	18-Oct-17	3,622	-	1,420	-	19-Aug-20		
	FY18 deferred STI	24-Aug-18	-	-	547	-	19-Aug-20		
	FY19 LTI	17-Oct-18	4,050	21,971	760	14,757	18-Aug-21		
	FY19 deferred STI	17-Sep-19	-	-	679	47,473	18-Aug-21		
	FY20 LTI	23-Oct-19	2,287	23,985	377	16,396	17-Aug-22		
	FY20 LTI	23-Oct-19	3,117	41,778	574	28,629	16-Aug-23		
	Total		**13,076**	**87,734**	**4,600**	**107,255**			
Jan Janssen	FY17 LTI	19-Oct-16	7,900	-	1,171	-	19-Aug-19	79.3%	20.7%
	FY17 deferred STI	24-Aug-17	-	-	867	-	19-Aug-19	100.0%	0.0%
	FY18 LTI	18-Oct-17	7,060	-	1,186	-	19-Aug-20		
	FY18 deferred STI	24-Aug-18	-	-	667	-	19-Aug-20		
	FY19 LTI	17-Oct-18	5,223	28,335	981	19,049	18-Aug-21		
	FY19 deferred STI	17-Sep-19	-	-	1,007	70,406	18-Aug-21		
	FY20 LTI	23-Oct-19	3,237	33,947	534	23,225	17-Aug-22		
	FY20 LTI	23-Oct-19	4,413	59,149	813	40,550	16-Aug-23		
	Total		**27,833**	**121,431**	**7,226**	**153,230**			
Tony Manna	FY17 LTI	19-Oct-16	9,414	-	598	-	19-Aug-19	79.3%	20.7%
	FY17 deferred STI	24-Aug-17	-	-	995	-	19-Aug-19	100.0%	0.0%
	FY18 LTI	18-Oct-17	10,385	-	436	-	19-Aug-20		
	FY18 deferred STI	24-Aug-18	-	-	645	-	19-Aug-20		
	FY19 LTI	17-Oct-18	7,530	40,850	353	6,854	18-Aug-21		
	FY19 deferred STI	17-Sep-19	-	-	841	58,800	18-Aug-21		
	FY20 LTI	23-Oct-19	3,055	32,039	504	21,920	17-Aug-22		
	FY20 LTI	23-Oct-19	4,165	55,825	767	38,256	16-Aug-23		
	Total		**34,549**	**128,714**	**5,139**	**125,830**			

1. The options granted in FY20 have an exercise price of $217.28, and an expiry date of 17 March 2023 (awards vesting after 3 years) and 16 March 2024 (awards vesting after 4 years). Fair values (IFRS-2) of FY20 options and performance rights under the LTI plan as at the date of grant are as follows:
   - options: 3 year (EPS growth: $34.13; relative TSR: $31.46) and 4 year (EPS growth: $37.56; relative TSR: $35.74); and
   - performance rights: 3 year (EPS growth: $206.70; relative TSR: $130.48) and 4 year (EPS growth: $203.72; relative TSR: $133.01).

   This valuation is for accounting purposes only and forms the basis of the expense in future years. Further detail on the allocation methodology is provided in section 3.4.

8.2 Executive KMP equity holdings and minimum shareholding

This section details the movement in equity holdings during the financial year.

Shares held during the year

During the year, the FY17 deferred STI plan and FY17 LTI plan vested in August 2019, and executives' options/rights converted into shares under these plans.

	Balance 1 July 2019	Received on exercise of options/rights[1]	Purchases and sales	Balance 30 June 2020
Executive KMP				
Dig Howitt	40,094	10,394	(8,013)	42,475
Anthony Bishop	752	2,912	(1,165)	2,499
Richard Brook	6,816	6,943	(8,759)	5,000
Brent Cubis	-	243	100	343
Jan Janssen	6,786	8,059	(8,059)	6,786
Tony Manna	2,182	8,934	(6,988)	4,128

1. For options exercised, the amount paid per option was the exercise price of $135.84.

Rights held during the year

Rights are acquired by executive KMP under the deferred STI and LTI plan. During the year:

- granted: FY19 STI deferred awards were granted in September 2019 (based on the FY19 performance year) and FY20 LTI awards were granted in October 2019; and
- vested: 100% of the FY17 deferred STI award and 79.3% of the FY17 LTI award vested in August 2019.

	Balance	Deferred STI service rights			LTI performance rights			Balance
	1 July 2019	Granted	Vested	Forfeited	Granted	Vested	Forfeited	30 June 2020
Executive KMP								
Dig Howitt	9,235	2,634	(949)	-	4,432	(1,218)	(319)	13,815
Anthony Bishop	3,184	582	(596)	-	838	(595)	(156)	3,257
Richard Brook	5,580	858	(944)	-	1,115	(1,541)	(403)	4,665
Brent Cubis	2,970	679	(243)	-	951	-	-	4,357
Jan Janssen	4,872	1,007	(867)	-	1,347	(928)	(243)	5,188
Tony Manna	3,027	841	(995)	-	1,271	(474)	(124)	3,546

Options held during the year

Options over ordinary shares are acquired by executive KMP under the LTI plan. During the year, FY20 LTI awards were granted in October 2019 and 79.3% of the FY17 LTI award vested in August 2019.

All options held at the end of the year are unvested.

	Balance	LTI options			Balance
	1 July 2019	Granted	Vested and exercised[1]	Forfeited	30 June 2020
Executive KMP					
Dig Howitt	93,124	24,041	(8,227)	(2,148)	106,790
Anthony Bishop	5,547	4,759	(1,721)	(450)	8,135
Richard Brook	17,152	6,331	(4,458)	(1,164)	17,861
Brent Cubis	7,672	5,404	-	-	13,076
Jan Janssen	20,183	7,650	(6,264)	(1,636)	19,933
Tony Manna	27,329	7,220	(7,465)	(1,949)	25,135

1. The value of exercised options at the date of vesting is $81.95 (closing share price at the vesting date 19 August 2019 of $217.79 less the exercise price of $135.84).

Executive minimum shareholding

As at 30 June 2020, the Board is satisfied that the executive KMP are compliant with the Share Ownership Policy. The table below presents a summary of executive KMP holdings and compliance with minimum shareholding requirements.

	Ordinary shares held	Policy value of Cochlear shares at year end ($)[1]	% of base salary[2]
Executive KMP			
Dig Howitt	42,475	8,923,148	518%
Anthony Bishop	2,499	524,990	97%
Richard Brook	5,000	1,050,400	137%
Brent Cubis	343	72,057	12%
Jan Janssen	6,786	1,425,603	172%
Tony Manna	4,128	867,210	106%

1. In line with the Share Ownership Policy, the value has been calculated as the average daily share price over the previous 12 months ($210.08), as at closing on the ASX up to 30 June 2020, times the number of shares.
2. The % of base salary is calculated as the value of shares divided by the actual base salary for the preceding 12 months to 30 June 2020.

8.3 Potential dilution if options vest and ordinary shares issued (unaudited)

The Board encourages employee ownership of Cochlear shares. To restrict dilution of shareholders' interests, the total employee interests in unvested equity cannot exceed 5% of share capital.

At the date of this report, the number of ordinary shares that would be issued if all options were vested, having met the service and performance conditions, and exercised and assuming ordinary shares were issued, is as follows.

	Grant date	Number of options			Exercise price per share ($)	Exercise period	Current net value of outstanding options as at 30 June 2020 ($)[2]
		Issued	Forfeited/ lapsed[1]	At report date			
FY18 LTI	18-Oct-17	106,713	2,337	104,376	154.73	Aug-20 to Mar-21	3,569,659
FY19 LTI	17-Oct-18	80,231	4,486	75,745	202.84	Aug-21 to Mar-22	-
FY20 LTI	23-Oct-19	24,231	-	24,231	217.28	Aug-22 to Mar-23	-
FY20 LTI	23-Oct-19	57,074	-	57,074	217.28	Aug-23 to Mar-24	-
Total		**268,249**	**6,823**	**261,426**			**3,569,659**

1. Forfeited/lapsed options from unvested grants relate to plan participants who have departed Cochlear.
2. Closing share price as at 30 June 2020 was $188.93.

Total unvested equity currently accounts for approximately 0.55% of the total number of issued shares, as set out below.

Instrument	Number of equivalent shares at 30 June 2020
Unvested LTI options	261,426
Unvested LTI rights	35,625
Unvested deferred STI rights	59,372
Service rights under the APAC Employee Equity Plan[1]	3,896
Total	**360,319**
as % of total issued shares	0.55%
Number of issued shares	65,687,402

1. Refer to Note 4.3 to the financial statements for further information on the APAC Employee Equity Plan.

8.4 Transactions and loans with KMP

No transactions or loans involving directors or executive KMP, their close family members or entities they control or have significant influence over, were made during the year.

9. Non-executive director fees

NEDs are paid from an aggregate annual fee pool for FY20 of $3,000,000 (approved at the 2017 Annual General Meeting). Total remuneration paid during the year was $2,325,215 which is within the fee pool limit (represented 77.5% of fee pool). NEDs do not receive any performance-related remuneration, options or performance rights. NEDs receive reimbursement for costs directly related to Cochlear business.

9.1 Fee policy and changes during the year

Board fees must recognise the effort required to fulfil the responsibilities of a director. Reflecting the increasing governance requirements and the work of the Board, the Board considered it appropriate to increase annual base fees by 2.5%, effective 1 July 2019. Committee fees remain unchanged. This decision was made with reference to external remuneration benchmarking of companies of a similar market capitalisation to that of Cochlear.

In response to the significant impact of COVID-19 on financial performance, the Board implemented a 30% reduction in Board and committee fees for a period of three months from mid-April 2020. There will be no fee increases for the Board for FY21.

The table below outlines the policy base and committee fees for FY19 and FY20.

Amounts $[1]	FY19		FY20	
	Chair	Member	Chair	Member
Cochlear Board	505,900	165,779	518,547	169,923
Committees[2]				
Audit & Risk	50,000	25,000	50,000	25,000
People & Culture	40,000	20,000	40,000	20,000
Technology & Innovation	40,000	20,000	40,000	20,000
Medical Science	30,000	15,000	30,000	15,000
Nomination	No fee	No fee	No fee	No fee

1. Superannuation contributions have been made in accordance with Australian superannuation legislation at a rate of 9.5% up to the Australian Government's prescribed maximum contributions limit. Fees are presented exclusive of superannuation.
2. Committee fees are not paid to the Chairman of the Board.

9.2 NED statutory remuneration

The table below presents the total remuneration for NEDs.

Amounts $	Year	Short-term benefits	Post-employment benefits	Total
		Fees	Superannuation[1]	
Rick Holliday-Smith	**FY20**	**488,387**	**21,003**	**509,390**
	FY19	505,617	20,531	526,148
Yasmin Allen	**FY20**	**244,848**	**21,003**	**265,851**
	FY19	255,686	20,531	276,217
Glen Boreham	**FY20**	**240,136**	**21,003**	**261,139**
	FY19	250,686	20,531	271,217
Michael Daniell[2]	**FY20**	**85,122**	**9,210**	**94,332**
	FY19	-	-	-
Alison Deans[3]	**FY20**	**249,022**	**10,501**	**259,523**
	FY19	230,686	20,384	251,070
Andrew Denver	**FY20**	**218,194**	**20,492**	**238,686**
	FY19	245,686	20,531	266,217
Abbas Hussain[4]	**FY20**	**193,021**	**19,280**	**212,301**
	FY19	111,973	10,635	122,608
Donal O'Dwyer	**FY20**	**216,578**	**20,492**	**237,070**

Amounts $	Year	Short-term benefits	Post-employment benefits	Total
		Fees	Superannuation[1]	
	FY19	225,686	20,165	245,851
Bruce Robinson	**FY20**	**226,002**	**20,921**	**246,923**
	FY19	235,686	20,531	256,217
Total	**FY20**	**2,161,310**	**163,905**	**2,325,215**
	FY19	2,061,706	153,839	2,215,545

The total fees for FY19 of $2,215,545 in this table is less than the total for FY19 in the 2019 Remuneration report of $2,745,148 as it does not include $529,603 for the former NED, Edward Byrne who retired as a NED on 16 October 2018.

1. During the temporary fee reduction period from mid-April 2020, superannuation was maintained on full fees, and continued to be capped at the maximum superannuation contribution limit.
2. Michael Daniell was appointed to the Board on 1 January 2020.
3. Effective 1 January 2020, Alison Deans has opted out of receiving superannuation guarantee payments in accordance with the *Superannuation Guarantee (Administration) Act 1992*. An equivalent amount of $10,501 was made over the period from 1 January 2020 to 30 June 2020 as fees.
4. Abbas Hussain was appointed to the Board on 1 December 2018.

9.3 Minimum shareholding requirement for NEDs

NEDs are requested to hold shares equivalent to the fees (including both Board and committee fees) received in the previous 12 months. The share ownership requirement must be satisfied within three years of appointment to the Board.

As at 30 June 2020, all NEDs are compliant with the Share Ownership Policy which allows three years to build their shareholdings. The table below presents Cochlear Limited shareholdings for each NED. All NEDs increased their shareholding through the Share Purchase Plan in April 2020.

	Balance 1 July 2019	Purchases	Sales	Balance 30 June 2020	Policy value of shares as at 30 June 2020 ($)[1]	% of fees
Rick Holliday-Smith	10,000	214	-	10,214	2,145,757	439%
Yasmin Allen	3,500	214	-	3,714	780,237	319%
Glen Boreham	2,800	214	-	3,014	633,181	264%
Michael Daniell[2]	-	1,214	-	1,214	255,037	300%
Alison Deans	3,000	214	-	3,214	675,197	271%
Andrew Denver	4,000	214	-	4,214	885,277	406%
Abbas Hussain[3]	-	226	-	226	47,478	25%
Donal O'Dwyer	6,000	214	-	6,214	1,305,437	603%
Bruce Robinson[4]	1,652	214	(933)	933	196,005	87%

1. In line with the Share Ownership Policy, available in the 'Investor Centre' section of the Company's website, the value of Cochlear Limited ordinary shares is calculated using the average daily share price over the previous 12 months ($210.08), as at closing on the ASX up to 30 June 2020, times the number of shares.
2. Michael Daniell was appointed to the Board on 1 January 2020. The % of fees has been calculated based on his actual total fees for the six-month period post appointment from 1 January 2020 to 30 June 2020.
3. Abbas Hussain was appointed to the Board on 1 December 2018, and in accordance with the policy has until 1 December 2021 to build his shareholding.
4. Bruce Robinson did an off-market transfer required by a Court Order in a family law settlement.

Directors' report

The directors present their report, together with the Consolidated Financial report of the Consolidated Entity (Cochlear), being Cochlear Limited (the Company) and its controlled entities, for the year ended 30 June 2020, and the Auditor's report thereon.

Directors

The directors of the Company at any time during or since the end of the financial year were Mr R Holliday-Smith (Chairman), Mrs YA Allen, Mr G Boreham, AM, Mr M Daniell, Ms A Deans, Mr A Denver, Mr D Howitt, Mr A Hussain, Mr DP O'Dwyer and Prof B Robinson, AC.

Information on the current directors is presented in the Annual Report. This information includes the qualifications, experience and special responsibilities of each director. It also gives details of the directors' other directorships.

Company Secretary

The Company Secretarial function is responsible for ensuring that the Company complies with its statutory duties and maintains proper documentation, registers and records. It also provides advice to directors and officers about corporate governance and gives practical effect to any decisions made by the Board.

Mr R Jarman was the Company Secretary during and since the end of the financial year. He has qualifications in law and science from The University of New South Wales and is an admitted solicitor in New South Wales. Mr Jarman joined Cochlear in 2008 as the inaugural Group General Counsel. He has over 35 years' experience in corporate and commercial law, litigation and dispute resolution, legal compliance and corporate governance across medical device, steel, mining and consumer goods industries.

Directors' meetings

The number of directors' meetings (including meetings of committees of directors) and number of meetings attended by each of the directors of the Company during the financial year are:

	Board of directors		Audit & Risk Committee		People & Culture Committee		Medical Science Committee		Nomination Committee		Technology & Innovation Committee	
	Held	Attended	Held	Attended	Held	Attended	Held	Attended	Held	Attended	Held	Attended
Mr R Holliday-Smith	21	21	5	5	4	4	-	-	4	4	-	-
Mrs YA Allen	21	20	5	5	4	4	-	-	4	3	3	2
Mr G Boreham, AM	21	21	5	5	4	4	-	-	4	4	3	3
Mr M Daniell[1]	15	14	-	-	-	-	-	-	1	1	1	1
Ms A Deans[2]	21	21	5	5	4	4	-	-	4	4	3	3
Mr A Denver[3]	21	21	5	5	-	-	2	2	4	4	3	3
Mr D Howitt	21	21	-	-	-	-	2	2	-	-	3	3
Mr A Hussain	21	19	-	-	-	-	2	-	4	2	3	2
Mr DP O'Dwyer	21	21	5	5	-	-	2	2	4	4	3	3
Prof B Robinson, AC	21	20	-	-	4	4	2	2	4	4	3	3

1. Mr Daniell was appointed on 1 January 2020.
2. Ms Deans was appointed as Chair of the Technology & Innovation Committee effective 23 July 2019.
3. Mr Denver ceased as Chair of the Technology & Innovation Committee from 23 July 2019.

Principal activities

Information on the principal activities, operations and financial position of Cochlear Limited and its business strategies and prospects is set out in the Operating and financial review on pages 15 to 32 of this Annual Report.

Dividends

Dividends declared and paid by the Company to members since the end of the previous financial year are:

	Dollars per share	Total amount $m	Franked/ unfranked	Date of payment
Interim 2020 ordinary	1.60	92.5	100% Franked	17 April 2020
Final 2019 ordinary	1.75	101.2	100% Franked	14 October 2019
Total amount	**3.35**	**193.7**		

No final dividend has been declared after 30 June 2020. Franked dividends declared and paid during the financial year were franked at the tax rate of 30% (2019: 30%).

Environmental regulations

Cochlear's operations are subject to environmental regulations under the Commonwealth of Australia and State/Territory legislation. The Board believes that Cochlear has adequate systems in place to manage its environmental obligations and is not aware of any breach of those environmental requirements as they apply to Cochlear.

Non-audit services

During the year, KPMG, the Company's auditor, performed certain other services in addition to its statutory duties. The Board has considered the non-audit services provided during the year by the auditor and in accordance with written advice provided by resolution of the Audit & Risk Committee, is satisfied that the provision of those non-audit services during the year by the auditor is compatible with, and did not compromise, the auditor independence requirements of the *Corporations Act 2001* for the following reasons:

- all non-audit services were subject to the corporate governance procedures adopted by the Company and have been reviewed by the Audit & Risk Committee to ensure that they do not impact the integrity and objectivity of the auditor; and
- the non-audit services provided do not undermine the general principles relating to auditor independence as set out in APES 110 Code of Ethics for Professional Accountants, as they did not involve reviewing or auditing the auditor's own work, acting in a management or decision-making capacity for the Company, acting as an advocate for the Company or jointly sharing risks and rewards.

Details of the amounts paid to the auditor of the Company, KPMG, and its related practices for audit and non-audit services during the year are set out below:

	Consolidated	
	2020	**2019**
	$	**$**
Audit services		
Audit and review of financial reports	2,170,767	1,809,019
Total audit services	**2,170,767**	**1,809,019**
Non-audit services		
Other assurance services	35,666	133,481
Taxation compliance and advisory services	1,547,505	1,764,533
IT advisory	-	643,260
Other	9,185	357,650
Total non-audit services	**1,592,356**	**2,898,924**

State of affairs

There were no significant changes to the state of affairs of Cochlear during the financial year other than that referred to in the financial statements or notes thereto.

Remuneration report

Information on Cochlear's remuneration framework and the outcomes for the financial year ended 30 June 2020 for the Cochlear Limited Board, the CEO & President and other key management personnel, and changes for the financial year ending 30 June 2021, is included in the Remuneration report on pages 40 to 57 of this Annual Report.

Indemnification of officers

Under the terms of Article 35 of the Company's Constitution, and to the extent permitted by law, the Company has indemnified the directors of the Company named in this Directors' report, the Company Secretary, Mr R Jarman, and other persons concerned in or taking part in the management of the Consolidated Entity. The indemnity applies when persons are acting in their capacity as officers of the Company in respect of:

- liability to third parties (other than the Company or related bodies corporate), if the relevant officer has acted in good faith; and
- costs and expenses of successfully defending legal proceedings in which relief under the *Corporations Act 2001* is granted to the relevant officer.

Insurance premiums

During the financial year, the Company paid a premium for a Directors' and Officers' Liability Insurance policy. The insurance provides cover for the directors named in this Directors' report, the Company Secretary, and officers and former directors and officers of the Company. The insurance also provides cover for present and former directors and officers of other companies in the Consolidated Entity. The directors have not included in this report details of the nature of the liabilities covered and the amount of the premium paid in respect of the Directors' and Officers' Liability and Supplementary Legal Expenses Insurance policies, as such disclosure is prohibited under the terms of the contract.

Events subsequent to the reporting date

Other than the matter noted below, there has not arisen in the interval between the end of the financial year and the date of this Directors' 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:

Patent litigation expense

Subsequent to year-end, Cochlear agreed to a settlement with Alfred E. Mann Foundation for Scientific Research and Advanced Bionics LLC (collectively referred to as AMF and AB) for pre-judgment interest and attorneys' fees totalling USD 75 million in the long-running patent dispute. At 30 June 2020, Cochlear has provided USD 75 million in relation to these claims which are also included in the patent litigation expense within the Income Statement. The settlement is conditional upon the outcome of an appeal by Cochlear to the US Supreme Court against the Judgment of USD 280 million in patent infringement damages and post judgment interest against the Defendants.

Cochlear has agreed to file its appeal by no later than 15 September 2020. Cochlear has also agreed to deposit USD 75 million into escrow account pending the outcome of the appeal. If Cochlear's Supreme Court appeal is unsuccessful, the monies in the escrow account will be paid to AMF and AB and the settlement will become final.

If Cochlear's Supreme Court appeal is successful, the monies in the escrow account will be returned to Cochlear and there may be a new trial to redetermine the quantum of damages.

Lead auditor's independence declaration

The lead auditor's independence declaration is set out on page 62 and forms part of the Directors' report for the financial year ended 30 June 2020.

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 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 stated.

Dated at Sydney this 18th day of August 2020.

Signed in accordance with a resolution of the directors:

Director

Director

Auditor’s independence declaration

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 audit for the year ended 30 June 2020 there have been:

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

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

KPMG

KPMG

Julian McPherson, Partner

Sydney, 18 August 2020

Income statement

	Note	2020 $m	2019 $m
Revenue	2.2	1,320.6	1,426.7
Cost of sales	2.3	(344.4)	(351.1)
Gross profit		**976.2**	**1,075.6**
Selling, marketing and general expenses		(470.0)	(450.9)
Research and development expenses		(185.1)	(184.4)
Administration expenses		(93.8)	(94.8)
Other income	2.4	78.1	29.0
Other expenses	2.3	(62.7)	(4.4)
Patent litigation expense	2.3	(503.7)	-
Share of losses on equity accounted investments	5.5	(1.2)	-
Results from operating activities		**(262.2)**	**370.1**
Finance income - interest		1.6	0.7
Finance expense - interest		(10.5)	(5.2)
Net finance expense		**(8.9)**	**(4.5)**
(Loss)/profit before income tax		**(271.1)**	**365.6**
Income tax benefit/(expense)	3.1	32.8	(88.9)
Net (loss)/profit		**(238.3)**	**276.7**
Basic (loss)/earnings per share (cents)	2.5	(399.6)	479.6
Diluted (loss)/earnings per share (cents)	2.5	(399.6)	479.5

The Consolidated Entity has initially applied AASB 16 Leases at 1 July 2019. Under the transition methods chosen, comparative information is not restated. See Note 5.8.

The notes on pages 68 to 105 are an integral part of these consolidated financial statements.

Statement of comprehensive income

	2020 $m	2019 $m
Net (loss)/profit	**(238.3)**	**276.7**
Other comprehensive income/(loss)		
Items that will not be reclassified subsequently to the income statement:		
Defined benefit plan actuarial gain/(losses)	1.6	(0.2)
Financial investments measured at fair value through other comprehensive income, net of tax	(1.8)	(1.3)
Total items that will not be reclassified subsequently to the income statement	**(0.2)**	**(1.5)**
Items that are or may be reclassified subsequently to the income statement:		
Foreign currency translation differences	3.9	12.6
Effective portion of changes in fair value of cash flow hedges, net of tax	(22.6)	(17.8)
Net change in fair value of discontinued cash flow hedges transferred to income statement, net of tax	18.3	-
Net change in fair value of cash flow hedges transferred to the income statement, net of tax	22.2	13.6
Total items that are or may be reclassified subsequently to the income statement	**21.8**	**8.4**
Total other comprehensive income, net of tax	**21.6**	**6.9**
Total comprehensive (loss)/income	**(216.7)**	**283.6**

The Consolidated Entity has initially applied AASB 16 Leases at 1 July 2019. Under the transition methods chosen, comparative information is not restated. See Note 5.8.

The notes on pages 68 to 105 are an integral part of these consolidated financial statements.

Balance sheet

	Note	2020 $m	2019 $m
Assets			
Cash and cash equivalents		565.0	78.6
Term deposits	6.3(b)	365.0	-
Trade and other receivables	6.4(b)	235.5	319.7
Forward exchange contracts		1.2	2.2
Inventories	5.1	223.8	195.4
Current tax assets	3.2	69.4	12.2
Prepayments		17.6	26.9
Total current assets		**1,477.5**	**635.0**
Other receivables		5.0	3.3
Forward exchange contracts		2.1	2.1
Property, plant and equipment	5.2	230.5	166.5
Intangible assets	5.3	410.3	424.4
Investments	5.4	25.9	47.8
Equity accounted investments	5.5	69.0	-
Deferred tax assets	3.2	147.1	100.1
Right of use asset	5.8	208.3	-
Total non-current assets		**1,098.2**	**744.2**
Total assets		**2,575.7**	**1,379.2**
Liabilities			
Trade and other payables		159.3	160.8
Forward exchange contracts		0.3	20.9
Loans and borrowings	6.3(a)	393.1	3.3
Current tax liabilities	3.2	7.2	34.8
Employee benefit liabilities	4.2	54.4	69.5
Provisions	5.6	130.2	27.3
Deferred revenue		47.0	42.9
Lease liability	5.8	26.0	-
Total current liabilities		**817.5**	**359.5**
Trade and other payables		13.6	42.4
Forward exchange contracts		1.7	7.6
Loans and borrowings	6.3(a)	79.9	178.3
Employee benefit liabilities	4.2	12.4	13.1
Provisions	5.6	27.2	44.2
Deferred tax liabilities	3.2	14.1	5.5
Deferred revenue		2.3	2.7
Lease liability	5.8	205.5	-
Total non-current liabilities		**356.7**	**293.8**
Total liabilities		**1,174.2**	**653.3**
Net assets		**1,401.5**	**725.9**
Equity			
Share capital		1,272.4	182.3
Reserves		12.7	(15.3)
Retained earnings		116.4	558.9
Total equity		**1,401.5**	**725.9**

The Consolidated Entity has initially applied AASB 16 Leases at 1 July 2019. Under the transition methods chosen, comparative information is not restated. See Note 5.8.

The notes on pages 68 to 105 are an integral part of these consolidated financial statements.

Statement of changes in equity

$m	Issued capital	Translation reserve	Hedging reserve	Fair value reserve	Share based payment reserve	Retained earnings	Total equity
2019							
Balance at 1 July 2018	173.0	(59.8)	(12.8)	0.2	39.0	464.2	603.8
Total comprehensive income/(loss)							
Net profit	-	-	-	-	-	276.7	276.7
Other comprehensive (loss)/income							
Defined benefit plan actuarial losses	-	-	-	-	-	(0.2)	(0.2)
Financial investments measured at fair value through other comprehensive income, net of tax	-	-	-	(1.3)	-	-	(1.3)
Foreign currency translation differences	-	12.6	-	-	-	-	12.6
Effective portion of changes in fair value of cash flow hedges, net of tax	-	-	(17.8)	-	-	-	(17.8)
Net change in fair value of cash flow hedges transferred to the income statement, net of tax	-	-	13.6	-	-	-	13.6
Total other comprehensive income/(loss)	**-**	**12.6**	**(4.2)**	**(1.3)**	**-**	**(0.2)**	**6.9**
Total comprehensive income/(loss)	**-**	**12.6**	**(4.2)**	**(1.3)**	**-**	**276.5**	**283.6**
Transactions with owners, recorded directly in equity							
Share options exercised	9.3	-	-	-	(1.8)	-	7.5
Performance rights vested	-	-	-	-	(0.1)	-	(0.1)
Share based payment transactions	-	-	-	-	8.5	-	8.5
Deferred tax recognised in equity	-	-	-	-	4.4	-	4.4
Dividends to shareholders	-	-	-	-	-	(181.8)	(181.8)
Balance at 30 June 2019	**182.3**	**(47.2)**	**(17.0)**	**(1.1)**	**50.0**	**558.9**	**725.9**
2020							
Balance at 1 July 2019 (as reported)	182.3	(47.2)	(17.0)	(1.1)	50.0	558.9	725.9
Change on initial application of AASB 16, net of tax	-	-	-	-	-	(12.1)	(12.1)
Balance at 1 July 2019 (restated)	**182.3**	**(47.2)**	**(17.0)**	**(1.1)**	**50.0**	**546.8**	**713.8**
Total comprehensive (loss)/income							
Net loss	-	-	-	-	-	(238.3)	(238.3)
Other comprehensive income/(loss)							
Defined benefit plan actuarial gains	-	-	-	-	-	1.6	1.6
Financial investments measured at fair value through other comprehensive income, net of tax	-	-	-	(1.8)	-	-	(1.8)
Foreign currency translation differences	-	3.9	-	-	-	-	3.9
Effective portion of changes in fair value of cash flow hedges, net of tax	-	-	(22.6)	-	-	-	(22.6)
Net change in fair value of discontinued cash flow hedges transferred to the income statement, net of tax	-	-	18.3	-	-	-	18.3
Net change in fair value of cash flow hedges transferred to the income statement, net of tax	-	-	22.2	-	-	-	22.2
Total other comprehensive income/(loss)	**-**	**3.9**	**17.9**	**(1.8)**	**-**	**1.6**	**21.6**
Total comprehensive income/(loss)	**-**	**3.9**	**17.9**	**(1.8)**	**-**	**(236.7)**	**(216.7)**
Transactions with owners, recorded directly in equity							
Share options exercised	7.4	-	-	-	(0.5)	-	6.9
Performance rights vested	-	-	-	-	(0.6)	-	(0.6)
Shares issued through institutional placement, net of related costs	856.2	-	-	-	-	-	856.2
Shares issued through share purchase plan, net of related costs	219.4	-	-	-	-	-	219.4
Share based payment transactions	-	-	-	-	7.0	-	7.0
Deferred tax recognised in equity	7.1	-	-	-	2.1	-	9.2
Dividends to shareholders	-	-	-	-	-	(193.7)	(193.7)
Balance at 30 June 2020	**1,272.4**	**(43.3)**	**0.9**	**(2.9)**	**58.0**	**116.4**	**1,401.5**

The Consolidated Entity has initially applied AASB 16 Leases at 1 July 2019. Under the transition methods chosen, comparative information is not restated. See Note 5.8. The notes on pages 68 to 105 are an integral part of these consolidated financial statements.

Statement of cash flows

	Note	2020 $m	2019 $m
Cash flows from operating activities			
Cash receipts from customers		1,403.7	1,448.5
Cash paid to suppliers and employees		(1,501.6)	(1,064.7)
Grant and other income received	2.4	5.5	7.4
Government assistance in respect of COVID-19 received	2.4	23.6	-
Interest received		1.6	0.7
Interest paid		(10.5)	(5.2)
Income taxes paid	3.1	(80.1)	(90.7)
Net cash (used in)/provided by operating activities	2.7(b)	**(157.8)**	**296.0**
Cash flows from investing activities			
Acquisition of leasehold improvements and plant and equipment	5.2	(92.9)	(59.9)
Acquisition of IT system costs	5.3	(18.5)	(26.7)
Acquisition of other intangible assets	5.3	(19.1)	(28.0)
Acquisition of investments		(14.2)	(23.2)
Acquisition of term deposits		(365.0)	-
Net cash used in investing activities		**(509.7)**	**(137.8)**
Cash flows from financing activities			
Repayments of borrowings		(130.0)	(405.6)
Proceeds from borrowings		420.9	439.1
Payments of lease liability		(24.6)	-
Net proceeds from exercise of share options and performance rights		6.3	7.4
Net proceeds from shares issued through institutional placement		856.2	-
Net proceeds from share purchase plan		219.4	-
Dividends paid	2.6	(193.7)	(181.8)
Net cash provided by/(used in) in financing activities		**1,154.5**	**(140.9)**
Net increase in cash and cash equivalents		**487.0**	**17.3**
Cash and cash equivalents, net of overdrafts at 1 July		78.6	61.5
Effect of exchange rate fluctuations on cash held		(0.6)	(0.2)
Cash and cash equivalents, net of overdrafts at 30 June		**565.0**	**78.6**

The notes on pages 68 to 105 are an integral part of these consolidated financial statements.

Notes to the financial statements

1. Basis of preparation

This section sets out the Company's accounting policies that relate to the financial statements as a whole. Where an accounting policy is specific to one note, the policy is described in the note to which it relates.

1.1 Reporting entity

Cochlear Limited (the Company) is a company domiciled in Australia. The consolidated financial statements of the Company as at and for the year ended 30 June 2020 comprise 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.

1.2 Basis of preparation

(a) Statement of compliance

The Financial report is a general purpose financial report which has been prepared in accordance with Australian Accounting Standards (AASBs) adopted by the Australian Accounting Standards Board and the *Corporations Act 2001*. The consolidated financial statements comply with International Financial Reporting Standards (IFRS) and Interpretations adopted by the International Accounting Standards Board.

The Board approved the consolidated financial statements on 18 August 2020.

(b) Coronavirus (COVID-19) impacts

Cochlear continues to satisfy solvency and going concern assumptions despite the financial impacts of COVID-19. During the year, Cochlear raised additional capital which netted proceeds of $1,075.6 million and strengthened Cochlear's capital position together with additional debt facilities. After payment of the interim dividend, Cochlear suspended dividend payments until trading conditions improve.

Cochlear has undertaken a number of actions to manage costs. During COVID-19, the business implemented a short-term reduction in pay for its Board, CEO & President (CEO&P) and Senior Executives and also implemented a hiring freeze and suspension of short-term Incentives. The business has reduced non-essential spending, including reducing marketing, travel and consultant expenditure and has reviewed and reduced capital expenditure, where possible.

However, an adverse decision in the patent litigation dispute, resulted in Cochlear achieving a net loss for the full year.

At 30 June 2020, Cochlear has $457.0 million in net cash (net of outstanding loan liabilities) and has access to a further $529.9 million in unutilised bank loan facilities. Cochlear has obtained debt covenant waivers for the leverage and interest cover ratio covenants for the June 2020 and December 2020 testing periods. These financial resources provide Cochlear with ability to continue to meet its financial obligations despite the negative economic effects of COVID-19.

(c) Basis of measurement

The consolidated financial statements have been prepared on the historical cost basis except for derivative financial instruments and financial investments measured at fair value. The fair value measurement method of derivative instruments and financial investments measured at fair value through other comprehensive income is discussed further in Note 6.4(d).

(d) Functional and presentation currency

These consolidated financial statements are presented in Australian dollars (AUD), which is the Company's functional currency.

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

(e) Foreign currency

Foreign currency transactions

Transactions in foreign currencies are translated to the respective functional currencies of entities at the foreign exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the reporting date are translated to the functional currency at the foreign exchange rate ruling at that date. Non-monetary assets and liabilities denominated in foreign currencies that are stated at historical cost are translated using the exchange rate at the date of the transaction. Non-monetary assets and liabilities denominated in foreign currencies that are stated at fair value are translated to the functional currency at the foreign exchange rates ruling at the date the fair value was determined.

Foreign exchange differences arising on translation are recognised in the income statement within other income and other expenses.

Financial statements of foreign operations

The assets and liabilities of foreign operations are translated to the Company's functional currency at foreign exchange rates ruling at the reporting date. The revenues and expenses of foreign operations are translated to the Company's functional currency at rates approximating the foreign exchange rates ruling at the dates of transactions.

Foreign currency differences arising from translation of controlled entities are recognised in the foreign currency translation reserve (translation reserve) in equity. When a foreign operation is disposed of, in part or in full, the relevant amount of its translation reserve is transferred to the income statement and reported as part of the gain or loss on disposal.

Foreign exchange gains and losses arising from a monetary item receivable from or payable to a foreign operation, the settlement of which is neither planned nor likely in the foreseeable future, are considered to form part of a net investment in a foreign operation and are recognised in other comprehensive income, and presented in the translation reserve.

(f) Use of judgements and estimates

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

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the financial year in which the estimate is revised and in any future years affected.

Management discussed with the Audit & Risk Committee the development, selection and disclosure of Cochlear's critical accounting policies and estimates and the application of these policies and estimates.

Information about critical judgements in applying accounting policies that have the most significant effect on the amounts recognised in the consolidated financial statements is included in the following notes:

Note 4.2 – Employee benefit liabilities

Note 4.3 – Share based payments

Note 5.3 – Intangible assets

Note 5.6 – Provisions

Note 5.7 – Contingent liabilities

Note 5.8 – Leases

Note 6.4 – Financial risk management.

(g) Basis of consolidation

Controlled entities

The Consolidated Entity controls an entity when it is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. The financial statements of controlled entities are included in the consolidated financial statements from the date that control commences until the date that control ceases.

Transactions eliminated on consolidation

Intra-group balances and transactions, and any unrealised income and expenses arising from intra-group transactions, are eliminated in preparing the consolidated financial statements.

Special purpose entities

Cochlear has established special purpose entities (SPEs) for investment purposes. A SPE is consolidated if Cochlear concludes that it controls the SPE. SPEs controlled by Cochlear were established under terms that impose strict limitations on decision-making powers of the SPE's management.

(h) Goods and services tax (GST)

Revenues, expenses and assets are recognised net of the amount of GST. Where the amount of GST incurred is not recoverable from the taxation authority, the GST is recognised as part of the cost of acquisition of the asset or as part of the expense.

Receivables and payables are stated with the amount of GST included. The net amount of GST recoverable from, or payable to, the relevant taxation authority is included as a current asset or liability in the balance sheet.

Cash flows are included in the statement of cash flows on a gross basis. The GST components of cash flows arising from investing and financing activities which are recoverable from, or payable to, the relevant taxation authority are classified as operating cash flows.

(i) Comparability

Comparative information is reclassified where appropriate to enhance comparability.

2. Performance for the year

2.1 Operating segments

Cochlear's three reportable segments, determined on a geographical basis, are the strategic business units of Cochlear. Segment results, assets and liabilities include items directly attributable to a segment, as well as those that can be allocated on a reasonable basis. Unallocated items comprise corporate and other net expenses and corporate and manufacturing assets and liabilities.

Performance is measured based on segment earnings before interest and income tax (EBIT) as included in the internal management reports that are reviewed by Cochlear's CEO&P, who is also the chief operating decision-maker.

Information about reportable segments

	Americas		EMEA[1]		Asia Pacific		Total	
	2020	2019	2020	2019	2020	2019	2020	2019
	$m	$m	$m	$m	$m	$m	$m	$m
Reportable segment revenue	650.3	688.6	479.6	519.2	222.4	238.3	**1,352.3**	**1,446.1**
Reportable segment EBIT	335.0	374.6	191.7	238.9	59.0	79.2	**585.7**	**692.7**
Reportable segment assets	353.7	257.7	247.6	261.4	148.2	143.5	**749.5**	**662.6**
Reportable segment liabilities	148.7	93.7	67.6	57.8	37.6	43.1	**253.9**	**194.6**
Other material items								
Depreciation and amortisation	10.8	2.2	5.6	1.7	5.6	1.4	**22.0**	**5.3**
Write-down in value of inventories	2.0	0.6	1.5	0.7	0.8	0.3	**4.3**	**1.6**
Acquisition of non-current assets	29.7	5.4	1.9	2.4	1.4	3.2	**33.0**	**11.0**

1. Europe, Middle East and Africa.

Reconciliations of reportable segment revenues, profit or loss, assets and liabilities and other material items

Revenues	Cochlear implants	Services (sound processor upgrades and other)	Total Cochlear implants	Acoustics (bone conduction and acoustic implants)	Reportable segment revenue	Foreign exchange loss on hedged sales	Consolidated revenue
	$m	$m	$m	$m	$m	$m	$m
2020	817.9	395.5	**1,213.4**	138.9	**1,352.3**	(31.7)	**1,320.6**
2019	845.1	427.2	**1,272.3**	173.8	**1,446.1**	(19.4)	**1,426.7**

Profit or loss	Reportable segment EBIT	Corporate and other net expenses	Foreign exchange loss on hedged sales	Net finance expense	Consolidated (loss)/profit before income tax
	$m	$m	$m	$m	$m
2020	585.7	(816.2)	(31.7)	(8.9)	**(271.1)**
2019	692.7	(303.2)	(19.4)	(4.5)	**365.6**

Assets and liabilities	Reportable segment assets	Corporate and manufacturing assets	Consolidated total assets	Reportable segment liabilities	Corporate and manufacturing liabilities	Consolidated total liabilities
	$m	$m	$m	$m	$m	$m
2020	749.5	1,826.2	**2,575.7**	253.9	920.3	**1,174.2**
2019	662.6	716.6	**1,379.2**	194.6	458.7	**653.3**

Other material items	Reportable segment total		Corporate and manufacturing total		Consolidated total	
	2020	**2019**	**2020**	**2019**	**2020**	**2019**
	$m	**$m**	**$m**	**$m**	**$m**	**$m**
Depreciation and amortisation	22.0	5.3	55.5	33.2	**77.5**	**38.5**
Write-down in value of inventories	4.3	1.6	15.4	5.0	**19.7**	**6.6**
Acquisition of non-current assets	33.0	11.0	97.0	162.5	**130.0**	**173.5**
Impairment of intangible assets	-	-	16.7	-	**16.7**	**-**
Patent litigation expense	-	-	503.7	-	**503.7**	**-**
Equity accounted losses	-	-	1.2	-	**1.2**	**-**

2.2 Revenue

Revenue from the sale of cochlear and acoustic implants and associated sound processors and accessories to customers is based on the contracted sales price. Revenue is recognised at the point in time when control passes to the customer with the exact timing dependent on the agreed sales terms for each contract. Revenue from product sales is also deferred based on the historical rates of product returns.

Revenue from the rendering of services, including ongoing customer support and software licensing are provided to customers over time. Where payments are received in advance, the agreed transaction price is initially deferred and progressively recognised over the life of the agreement as the service is provided. The value of unfulfilled performance obligations under these contracts is reflected in the Consolidated Entity's deferred revenue balance.

Customers include implant recipients, medical practitioners and governments. Contracts are short-term with the exemption of software licences which are recognised over multiple years. The accounting policy for foreign exchange gains/losses arising from hedges of forecast sales transactions is set out in Note 6.4(a).

	2020 $m	2019 $m
Sale of goods before hedging	1,320.3	1,415.3
Foreign exchange loss on hedged sales	(31.7)	(19.4)
Revenue from sale of goods	**1,288.6**	**1,395.9**
Rendering of services	32.0	30.8
Total revenue	**1,320.6**	**1,426.7**

2.3 Expenses

	2020 $m	2019 $m
(a) Cost of sales		
Carrying amount of inventories recognised as an expense	329.7	337.8
Write-down in value of inventories[1]	8.2	6.6
Other	6.5	6.7
Total cost of sales	**344.4**	**351.1**

1. Total inventory write-down of $19.7 million comprises $8.2 million write-down of inventories in cost of sales and $11.5 million write-down of inventories in other expenses.

(b) (Loss)/profit before income tax has been arrived at after charging the following items:

	2020	2019
Operating lease rental expense	-	29.4
Patent litigation expense	503.7	-

Due to the adoption of AASB 16 Leases, operating lease rental expenses are replaced by amortisation of the right of use assets and interest expense, refer to Note 5.8.

Patent litigation expense

In March 2020, the US Court of Appeals affirmed the US District Court's decision 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 and Advanced Bionics LLC (collectively referred to as AMF and AB). The affirmation resulted in the Defendants paying USD 268 million in relation to patent infringement damages and a further USD 12 million in post judgment interest. At 30 June 2020, the Defendants have paid the damages and interest awarded against it which have been expensed in the Income Statement. The Defendants intend to lodge an appeal with the US Supreme Court against the Judgment.

Subsequent to year-end, the Defendants agreed to a settlement with AMF and AB of pre-judgment interest and attorneys' fees totalling USD 75 million. At 30 June 2020, Cochlear has provided USD 75 million in relation to this settlement which is included in the patent litigation expense within the Income Statement. The settlement is conditional upon the outcome of an appeal by the Defendants to the US Supreme Court against the Judgment of USD 280 million for patent infringement damages and post judgment interest.

The Defendants have agreed to file their appeal by no later than 15 September 2020. The Defendants have also agreed to deposit USD 75 million into an escrow account pending the outcome of the appeal. If the Defendants' Supreme Court appeal is unsuccessful, the monies in the escrow account will be paid to AMF and AB and the settlement will become final.

If the Defendants' Supreme Court appeal is successful, the monies in the escrow account will be returned to the Defendants and there may be a new trial to redetermine the quantum of damages.

Other expenses

	Note	2020 $m	2019 $m
Foreign exchange loss		6.8	4.4
Ineffective forward exchange contracts	6.4(a)	26.1	-
Impairment expense[1]		29.8	-
Total other expenses		**62.7**	**4.4**

1. Impairment expense includes $11.5 million of inventory write-downs.

2.4 Other income

Other income, including government grants, is recognised on a systematic basis over the years necessary to match it with the related costs for which it is intended to compensate. If the costs have already been incurred, the amount is recognised in the year the entitlement is confirmed. Foreign exchange gains/losses are recognised in accordance with the accounting policy at Note 1.2(e).

Due to the impact of COVID-19, Cochlear has received AUD 23.6 million in government assistance through the United States' Coronavirus Aid, Relief, and Economic Security Act ('CARES Act'), Australia's JobKeeper Program and other government assistance programs offered in Europe and Asia.

Changes to the contingent consideration value recognised for the Sycle, LLC business acquisition were considered at 30 June 2020. Based on FY20 revenue growth relative to the performance hurdle, $13.2 million (2019: $10.8 million) has been released to the income statement and $6.2 million remains as contingent consideration (2019: $19.4 million).

	2020 $m	2019 $m
Grant received or due and receivable	1.4	1.9
Release of contingent consideration	13.2	10.8
Government assistance in respect of COVID-19	23.6	-
Fair value change in investments measured at fair value through profit or loss	35.8	10.8
Other income	4.1	5.5
Total other income	**78.1**	**29.0**

2.5 Earnings per share

Cochlear presents basic and diluted earnings per share (EPS) for its ordinary shares.

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:

	2020	2019
Net (loss)/profit attributable to equity holders of the parent entity	($238,285,000)	$276,697,000
Weighted average number of ordinary shares (basic):		
Issued ordinary shares at 1 July (number)	57,715,821	57,547,820
Effect of options, performance shares and performance rights exercised (number)	88,382	134,937
Effect of shares issued under Employee Share Plan (number)	5,629	5,448
Effect of shares issued under institutional placement (number) [1]	1,562,842	-
Effect of shares issued under share purchase plan (number) [2]	261,928	-
Weighted average number of ordinary shares (basic) at 30 June	**59,634,602**	**57,688,205**
Basic (loss)/earnings per share (cents)	**(399.6)**	**479.6**

1. Institutional placement of 6,285,715 shares 31 March 2020, weighted as per days held for the purpose of the EPS calculation.
2. Share purchase plan of 1,571,567 shares 30 April 2020, weighted as per days held for the purpose of the EPS calculation.

Diluted earnings per share

The calculation of diluted EPS has been based on the following net (loss)/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:

	2020	2019
Net (loss)/profit attributable to equity holders of the parent entity	($238,285,000)	$276,697,000
Weighted average number of ordinary shares (diluted):		
Weighted average number of shares (basic) (number)	59,634,602	57,688,205
Effect of options, performance shares and performance rights unvested (number)	-	21,948
Weighted average number of ordinary shares (diluted) at 30 June	**59,634,602**	**57,710,153**
Diluted (loss)/earnings per share (cents)	**(399.6)**	**479.5**

2.6 Dividends

A liability for dividends payable is recognised in the financial year in which the dividends are declared.

	Dollars per share	Total amount $m	Franked/unfranked	Date of payment
Dividends recognised in the current financial year by the Company are:				
2020				
Interim 2020 ordinary	1.60	92.5	100% Franked	17 April 2020
Final 2019 ordinary	1.75	101.2	100% Franked	14 October 2019
Total amount	**3.35**	**193.7**		
2019				
Interim 2019 ordinary	1.55	89.5	100% Franked	16 April 2019
Final 2018 ordinary	1.60	92.3	100% Franked	10 October 2018
Total amount	**3.15**	**181.8**		

No final dividend has been declared after 30 June 2020.

Dividend franking account

Franked dividends paid during the financial year were franked at the tax rate of 30% (2019: 30%). There are no further tax consequences as a result of paying dividends other than a reduction in the franking account.

The dividend franking account at year end is normally adjusted for:

- franking credits that will arise from the payment of the current tax liability;
- franking debits that will arise from the payment of dividends recognised as a liability at the year end; and
- franking credits that the Company may be prevented from distributing in subsequent financial years.

At 30 June 2020, no franking credits will arise for the payment of a current tax liability and no final dividend has been declared after 30 June 2020.

As a result of no franking credits arising at year end, there are $0 million of franking credits (2019: $39.2 million) available to shareholders of Cochlear Limited for subsequent financial years.

The ability to utilise the franking account credits is dependent upon the ability to declare dividends. As no final 2020 dividend has been declared, there is no impact on the dividend franking account after the balance sheet date (2019: $43.3 million).

2.7 Notes to the statement of cash flows

(a) Cash and cash equivalents

Cash and cash equivalents comprise cash balances and call deposits with an original maturity of three months or less. Bank overdrafts that are repayable on demand and form an integral part of Cochlear's cash management are included as a component of cash and cash equivalents for the purpose of the statement of cash flows.

The operating cash account received an average interest rate of 1.09% (2019: 0.79%) per annum.

(b) Reconciliation of net (loss)/profit to net cash (used in)/provided by operating activities

	2020 $m	2019 $m
Net (loss)/profit	(238.3)	276.7
Add item classified as investing activities:		
Loss on disposal of property, plant and equipment	0.4	0.5
Add/(less) non-cash items:		
Depreciation and amortisation	77.5	38.5
Impairment of intangible assets	16.7	-
Release of contingent consideration	(13.2)	(10.8)
Change in fair value measurement of investments through profit or loss	(35.8)	(10.8)
Equity settled share based payment transactions	7.0	8.5
Share of losses on equity accounted investments	1.2	-
Net cash (used in)/provided by operating activities before changes in assets and liabilities	**(184.5)**	**302.6**
Changes in assets and liabilities:		
Change in trade and other receivables	82.5	(4.2)
Change in inventories	(28.4)	(28.0)
Change in prepayments	9.3	(1.6)
Change in deferred tax assets/liabilities	(38.4)	(22.0)
Change in trade and other payables	(30.3)	34.6
Change in current tax assets/liabilities	(84.8)	10.1
Change in employee benefit liabilities	(15.8)	13.3
Change in provisions	85.9	(7.4)
Change in deferred revenue	3.7	16.5
Effect of movements in foreign exchange	43.0	(17.9)
Net cash (used in)/provided by operating activities	**(157.8)**	**296.0**

3. Income taxes

The Company and its wholly owned Australian resident entities are part of a tax consolidated group. As a consequence, all members of the tax consolidated group are taxed as a single entity. The head entity within the tax consolidated group is Cochlear Limited.

3.1 Income tax (benefit)/expense

Income tax (benefit)/expense includes current and deferred tax. Current and deferred tax is recognised in the income statement except to the extent that they relate to items recognised directly in other comprehensive income or equity.

Current tax is the expected tax payable or receivable on the taxable income or loss for the year and any adjustment to tax payable in respect of previous years. It is measured using tax rates enacted or substantively enacted at the reporting date.

Income tax (benefit)/expense recognised in the income statement

	Current year	Adjustment for prior years	**Total current tax expense**	Origination and reversal of temporary differences	**Total deferred tax benefit**	**Total income tax (benefit)/ expense**
	$m	$m	**$m**	$m	**$m**	**$m**
2020	6.0	(2.7)	**3.3**	(36.1)	**(36.1)**	**(32.8)**
2019	105.0	(1.4)	**103.6**	(14.7)	**(14.7)**	**88.9**

Consolidated Entity - Numerical reconciliation between income tax (benefit)/expense and (loss)/profit before income tax

	2020 $m	2019 $m
(Loss)/profit before income tax	**(271.1)**	**365.6**
Tax at the Australian tax rate of 30% (2019: 30%)	(81.3)	109.7
Add/(less) adjustments for:		
Patent litigation	63.7	-
Other net non-assessable items	(3.3)	(3.4)
Research and development allowances	(9.4)	(9.7)
Effect of tax rates in foreign jurisdictions	0.2	(6.3)
	(30.1)	**90.3**
Adjustment for prior years	(2.7)	(1.4)
Income tax (benefit)/expense on (loss)/profit before income tax	**(32.8)**	**88.9**

Tax expense/(benefit) for items relating to other comprehensive income/(loss) or equity

	Note	2020 $m	2019 $m
Total deferred tax recognised in other comprehensive income/(loss) relating to derivative financial instruments	3.2	7.7	(1.8)
Total deferred tax recognised directly in equity relating to share based payments	3.2	(2.1)	(4.4)
Total deferred tax recognised directly in equity relating to capital raising	3.2	(7.1)	-

Consolidated Entity - Numerical reconciliation between income tax (benefit)/expense and cash taxes paid

	2020 $m	2019 $m
Income tax (benefit)/expense on (loss)/profit before income tax	(32.8)	88.9
Timing differences recognised in deferred tax	33.2	12.5
Effect of tax rates in foreign jurisdictions	0.6	0.3
Current year tax instalments refundable/(payable) next year	53.1	(26.0)
Prior year tax instalments paid this year	26.0	15.0
Cash taxes paid per statement of cash flows	**80.1**	**90.7**

Cochlear Limited's Australian tax consolidated group - Numerical reconciliation between income tax (benefit)/expense and (loss)/profit before income tax

	2020 $m	2019 $m
(Loss)/profit before income tax (excluding dividends from wholly owned foreign subsidiaries)	(306.4)	300.5
Add: Dividends from wholly owned foreign subsidiaries	116.0	6.9
(Loss)/profit before income tax	**(190.4)**	**307.4**
Tax at the Australian tax rate of 30% (2019: 30%)	(57.1)	92.2
Add/(less) adjustments for:		
Patent litigation	63.7	-
Other net (non-assessable)/non-deductible items	(1.7)	0.6
Controlled foreign company income	1.6	0.7
Research and development allowances	(8.5)	(8.5)
Exempt foreign sourced dividends from wholly owned subsidiaries	(34.8)	(2.1)
	(36.8)	**82.9**
Adjustment for prior years	(0.3)	(1.6)
Income tax (benefit)/expense on (loss)/profit before income tax	**(37.1)**	**81.3**

3.2 Current and deferred tax assets and liabilities

Deferred tax is recognised on all temporary differences between the carrying amounts of assets and liabilities for financial reporting and taxation purposes.

The measurement of deferred tax mirrors the tax consequences that the Consolidated Entity expects to recover or settle from the carrying amount of its assets and liabilities.

Deferred tax is measured at the tax rates that are expected to be applied to temporary differences when they reverse.

A deferred tax asset is recognised to the extent that it is probable that future taxable profits will be available against which they can be utilised. Deferred tax assets are reviewed at each reporting date and are reduced if it is no longer probable that the related tax benefit will be realised.

Recognised deferred tax assets and liabilities

	Assets		Liabilities		Net	
	2020 $m	2019 $m	2020 $m	2019 $m	2020 $m	2019 $m
Property, plant and equipment	5.1	0.4	(6.3)	(2.2)	(1.2)	(1.8)
Intangible assets	1.6	0.8	(3.0)	(6.5)	(1.4)	(5.7)
Inventories	46.9	40.8	-	-	46.9	40.8
Provisions	59.7	33.0	-	-	59.7	33.0
Deferred revenue	4.0	5.3	-	(2.5)	4.0	2.8
Forward exchange contracts	-	7.4	(0.4)	-	(0.4)	7.4
Tax losses and offsets carried forward	26.8	-	-	-	26.8	-
Other	10.4	20.4	(11.8)	(2.3)	(1.4)	18.1
Deferred tax assets/(liabilities)	**154.5**	**108.1**	**(21.5)**	**(13.5)**	**133.0**	**94.6**
Set off tax	(7.4)	(8.0)	7.4	8.0	-	-
Deferred tax assets/(liabilities)	**147.1**	**100.1**	**(14.1)**	**(5.5)**	**133.0**	**94.6**

Unrecognised deferred tax liabilities

At 30 June 2020, a deferred tax liability of $22.8 million (2019: $12.0 million) relating to investments in subsidiaries has not been recognised because the Company controls whether the asset will be recovered or the liability will be incurred and it is satisfied that it will not be incurred in the foreseeable future.

Movement in temporary differences during the year

	Note	2020 $m	2019 $m
Carrying amount at beginning of financial year		94.6	72.6
Recognised in the income statement	3.1	36.1	14.7
Recognised in other comprehensive income/(loss)	3.1	(7.7)	1.8
Recognised directly in equity	3.1	9.2	4.4
Effect of movements in foreign exchange		0.8	1.1
Carrying amount at end of financial year		**133.0**	**94.6**

Current tax assets and liabilities

The current tax assets for the Consolidated Entity of $69.4 million (2019: $12.2 million) represent the amount of income taxes recoverable in respect of current and prior years and arise from the payment of tax in excess of the amounts due to the relevant taxation authority. The current tax liabilities for the Consolidated Entity of $7.2 million (2019: $34.8 million) represent the amount of income taxes payable in respect of current and prior financial years.

4. Employee benefits

4.1 Employee expenses

	2020 $m	2019 $m
Wages and salaries	415.6	378.1
Contributions to superannuation plans	31.3	31.6
Increase in leave liabilities	6.4	6.9
Equity settled share based payment transactions	7.0	8.5
Total employee expenses	**460.3**	**425.1**

4.2 Employee benefit liabilities

Wages, salaries and annual leave

Liabilities for employee benefits for wages, salaries and annual leave are recognised in other payables and provisions if Cochlear has a present obligation to pay an amount as a result of past services provided by the employee. The liability is calculated on remuneration rates as at the reporting date including related on-costs, such as workers' compensation insurance and payroll tax.

Long service leave

The provision for long service leave is the present value of the estimated future cash outflows as a result of services provided by the employee up to the reporting date.

The provision is calculated using expected future increases in remuneration rates, including related on-costs, and expected settlement dates based on turnover history, and is discounted using the corporate bond rates which most closely match the terms to maturity of the related liabilities.

Defined benefit plans

The Consolidated Entity has defined benefit plans that cover, in aggregate, 84 employees in two countries (2019: 87 employees). Cochlear contributed cash of $1.5 million (2019: $1.3 million) to defined benefit plans in the year ended 30 June 2020 and expects to contribute $1.5 million in the year ending 30 June 2021.

The defined benefit obligations are calculated annually by a qualified actuary using the projected unit credit method. Remeasurements of the net defined benefit liability (excluding interest) are recognised immediately in other comprehensive income.

The Company determines the net interest expense/(income) on the net defined benefit liability/(asset) for the period by applying the discount rate used to measure the defined benefit obligation at the beginning of the period to the opening net defined benefit liability/(asset), adjusted for any changes in the net defined benefit liability/(asset) during the period resulting from contributions and benefit payments. Net interest expense related to defined benefit plans is recognised in the income statement.

Directors' retirement scheme

Non-executive directors appointed prior to 2003 were entitled to retirement benefits of up to three times their annual remuneration over the previous three years once they had more than five years' service. The ongoing accrual of benefits under the directors' retirement scheme ceased from 30 June 2007. The benefits accrued to that date are indexed by reference to the bank bill rate. There are no executive directors entitled to this benefit.

	2020 $m	2019 $m
Current		
Provision for long service leave	13.4	12.9
Provision for annual leave	36.3	31.0
Provision for short-term incentives and sales commissions	4.7	25.6
Total current employee benefit liabilities	**54.4**	**69.5**
Non-current		
Provision for long service leave	6.9	6.4
Defined benefit plan	5.5	6.7
Total non-current employee benefit liabilities	**12.4**	**13.1**
Total employee benefit liabilities	**66.8**	**82.6**

4.3 Share based payments

From 1 July 2013, the Company grants options and performance rights to certain employees under the Cochlear Executive Incentive Plan (CEIP).

The fair value of options and performance rights granted is recognised as an employee expense, with a corresponding increase in equity. The expense is adjusted by the actual number of options and rights that are expected to vest except where forfeiture is due to market related conditions.

The fair value is measured using the Black-Scholes-Merton pricing model at the date the options or performance rights are granted, taking into account market based criteria and the terms and conditions attached to the instruments. The options or performance rights are expensed over the vesting period after which the employees become unconditionally entitled to them.

When the Company grants options over its shares to employees of controlled entities, the fair value at grant date is recognised as an increase in the investment in subsidiaries, with a corresponding increase in equity over the vesting period of the grant in the Company's accounts. At 30 June 2020, the unissued ordinary shares of the Company under option and rights and the terms and conditions of the grants and issues are as follows:

Grant date	Exercise price of options	Number of options	Number of performance rights	Contractual life
October 2017[1]	$154.73	104,376	11,835	4 years
August 2018[2]	n/a	-	26,688	2 years
October 2018[1]	$202.84	75,745	9,280	4 years
September 2019[2]	n/a	-	32,684	2 years
October 2019[1,3]	$217.28	24,231	3,994	4 years
October 2019[1,3]	$217.28	57,074	10,516	5 years
Total		**261,426**	**94,997**	

1. Options and performance rights offered under long-term incentives (LTI).
2. Performance rights offered under deferred short-term incentives (STI).
3. FY20, LTI Award is subject to a four-year performance period and as a transition for FY20 LTI plan, 2 grants were offered including three-year and four-year performance period. No transitional arrangements were provided to the CEO&P. The CEO&P's FY20 LTI grant had a four- year performance period only.

Grants are split between deferred short-term incentives (STI) and long-term incentives (LTI).

For deferred STI, certain employees under the CEIP are granted performance rights based on achievement of a mandatory portion of their STI. The number of performance rights under the deferred STI grants is calculated at the end of each year and then held for two years until vesting.

Grants under LTI are in two equal tranches assigned to compound annual growth in EPS and ranking of total shareholder return (TSR) against the ASX 100 index. The conditions for minimum vesting are four years of service and:

- 50% weighting on compound annual growth rate (CAGR) in EPS with a minimum CAGR in EPS of 7.5% assigned to 50% of grant; or
- 50% weighting on relative TSR with the Consolidated Entity's TSR at the 50th percentile against the ASX 100 over four years assigned to 40% of grant.

For FY20, a transitional arrangement was implemented to recognise that increasing the performance period from three to four years, will result in a gap year of LTI vesting in FY22 for executives. For FY20 only, two grants were provided to the executive team (excluding the CEO&P):

- Grant 1: 50% of the annual LTI grant opportunity with a three-year performance period; and
- Grant 2: 75% of the annual LTI grant opportunity with a four-year performance period.

No transitional arrangement was provided to the CEO&P. The CEO&P's FY20 LTI grant opportunity continued to be 100% of base salary with a four-year performance period.

The grant date fair value of options and performance rights was measured based on the Black-Scholes-Merton pricing model. Gross contract value discounts for dividends not paid, share price volatility and the risk free rate of return. There is no discount for the likelihood of service or performance conditions. The model uses Cochlear's five-day volume-weighted average price following the announcement of full year results in August each year. The inputs used in the measurement of the fair values at the grant date are the following:

	23 October 2019 (3yr)		**23 October 2019 (4yr)**		**17 September 2019**	**17 October 2018**		**24 August 2018**
	TSR based conditions	**EPS performance based conditions**	**TSR based conditions**	**EPS performance based conditions**	**Deferred STI service based conditions**	**TSR based conditions**	**EPS performance based conditions**	**Deferred STI service based conditions**
Fair value of options at grant date	$31.46	$34.13	$35.74	$37.56	n/a	$32.55	$37.43	n/a
Fair value of performance rights at grant date	$130.48	$206.70	$133.01	$203.72	$209.75	$116.51	$199.29	$201.99
Share price at valuation date	$215.89	$215.89	$215.89	$215.89	$215.89	$207.50	$207.50	$207.50
Option exercise price	$217.28	$217.28	$217.28	$217.28	n/a	$202.84	$202.84	n/a
Expected volatility[1]	24.1%	24.1%	23.96%	23.96%	24.42%	22.59%	22.59%	22.59%
Option life (years)	3 - 4	3 - 4	4 -5	4 - 5	2	3 - 4	3 - 4	2
Expected dividend yield	1.46%	1.46%	1.46%	1.46%	1.46%	1.35%	1.35%	1.35%
Risk free interest rate[2]	0.71%	0.71%	0.71%	0.71%	0.71%	2.04%	2.04%	2.04%

1. Measure captures the characteristics of fluctuations in the share price.
2. Based on government bonds.

The number and weighted average exercise prices of options are as follows:

	Weighted average exercise price 2020	Number of options 2020	Weighted average exercise price 2019	Number of options 2019
Outstanding at 1 July	**$163.71**	**263,613**	**$119.60**	**318,227**
Forfeited	$150.26	(20,846)	$82.89	(4,724)
Exercised	$135.84	(62,646)	$82.89	(130,121)
Granted	$217.28	81,305	$202.84	80,231
Outstanding at 30 June	**$188.12**	**261,426**	**$163.71**	**263,613**
Exercisable at 30 June	$154.73	104,376	$135.84	79,006

62,646 options were exercised in 2020 (2019: 130,121 options were exercised). The weighted average market share price on the Australian Securities Exchange (ASX) at date of exercise was $215.30 (2019: $196.26). The weighted average remaining contractual life of options outstanding at the end of the year is two years (2019: two years).

Employee Share Plan

Cochlear's Employee Share Plan (Plan) was approved by special resolution at the Annual General Meeting held on 19 October 1999. Under the Plan, the directors can at their discretion, allocate at nil consideration up to a maximum of $2,000 worth of shares per eligible employee in any one year. In practice, the directors issue shares worth up to the tax concessional limit, currently approximately $1,000 per eligible employee each year. The fair value of shares issued during the financial year is the market price of the Company's shares on the ASX as at the start of trading on the issue date.

Shares under the Plan vest with the employee immediately but are non-transferable for a period of up to three years. For the year ended 30 June 2020, the Company issued 7,955 shares (2019: 7,590 shares) under the Plan, see Note 6.2.

APAC Employee Equity Plan

The APAC Employee Equity Plan, established in 2016, aligns with the Cochlear Employee Share Plan and provides up to approximately $1,000 of service rights annually per eligible employee in selected Asian countries. Upon vesting, each service right converts to one share. For the year ended 30 June 2020, the Company issued 826 shares under the plan (2019: 1,092 shares).

4.4 Key management personnel

The following were key management personnel (KMP) of Cochlear at any time during the financial year and unless otherwise indicated were KMP for the entire financial year:

Non-executive directors

Mr R Holliday-Smith (Chairman), Mrs YA Allen, Mr G Boreham, AM, Mr M Daniell[1], Ms A Deans, Mr A Denver, Mr A Hussain, Mr DP O'Dwyer and Prof B Robinson, AC

Executive KMP

Mr D Howitt, Mr A Bishop, Mr R Brook, Mr B Cubis, Mr J Janssen and Mr T Manna.

1. Appointed on 1 January 2020.

Key management personnel disclosures

The KMP compensation is included in employee expenses as follows:

	Short-term employee benefits $	Post-employment benefits $	Other long-term benefits $	Directors' retirement benefits[1] $	Share based payments $	Total $
2020	7,772,881	422,082	56,866	-	2,007,193	**10,259,022**
2019	10,340,814	414,161	8,857	461,136	2,150,552	**13,375,520**

1. Prof E Byrne retired from the Board on 16 October 2018.

Information regarding individual KMP remuneration and some equity instruments disclosures as permitted by section 300A of the *Corporations Act 2001* is provided in the Remuneration report of this Annual Report on pages 40 to 57.

The KMP have not received any loans from Cochlear and there have been no other related party transactions with any of Cochlear's KMP.

5. Operating assets and liabilities

5.1 Inventories

Inventories are measured at the lower of cost and net realisable value.

Cost is based on the first-in-first-out principle including expenditure incurred in acquiring the inventories and bringing them to their existing condition and location. In the case of manufactured inventories and work in progress, cost includes an appropriate share of production overheads based on normal operating capacity.

Net realisable value is the estimated selling price in the ordinary course of business less estimated costs of completion and selling, marketing and distribution expenses.

	Raw materials $m	Work in progress $m	Finished goods $m	Total inventories $m
2020	82.6	32.5	108.7	223.8
2019	70.3	26.2	98.9	195.4

5.2 Property, plant and equipment

Owned assets

The value of property, plant and equipment is measured as the cost of the asset, minus accumulated depreciation and impairment losses (see Note 5.3). The cost of the asset is the consideration provided plus incidental costs directly attributable to the acquisition.

The value of internally-constructed assets includes the cost of material and direct labour and any other costs directly attributable to bringing the asset to a working condition for its intended use.

Subsequent costs in relation to replacing a part of property, plant and equipment are capitalised in the carrying amount of the item if it is probable that future economic benefits will flow to Cochlear and its cost can be measured reliably. All other costs are recognised in the income statement as incurred.

Depreciation

Depreciation is calculated to expense the cost of items of property, plant and equipment less their estimated residual values on a straight-line basis over their estimated useful lives. The estimated useful lives in the current and comparative years are as follows: leasehold improvements between one to 15 years, plant and equipment between three to 14 years and buildings between 10 to 30 years.

Depreciation is recognised in the income statement from the date of acquisition or, in respect of internally-constructed assets, from the time an asset is completed and held ready for use.

Depreciation rates and methods, useful lives and residual values are reviewed at each balance sheet date. When changes are made, adjustments are reflected prospectively in current and future financial years only.

	Leasehold improvements		Plant and equipment		Land and buildings		Total	
	2020 $m	2019 $m	2020 $m	2019 $m	2020 $m	2019 $m	2020 $m	2019 $m
At cost	67.6	42.0	333.4	277.5	30.0	30.1	431.0	349.6
Accumulated depreciation	(28.7)	(28.2)	(171.2)	(154.4)	(0.6)	(0.5)	(200.5)	(183.1)
Net book value	**38.9**	**13.8**	**162.2**	**123.1**	**29.4**	**29.6**	**230.5**	**166.5**
Reconciliations of the carrying amounts are:								
Opening balance	13.8	13.3	123.1	85.3	29.6	29.8	166.5	128.4
Additions	30.0	3.3	62.9	56.6	-	-	92.9	59.9
Disposals	-	-	(0.4)	(0.5)	-	-	(0.4)	(0.5)
Depreciation	(4.4)	(3.2)	(22.0)	(19.5)	(0.2)	(0.2)	(26.6)	(22.9)
Effect of movements in foreign exchange	(0.5)	0.4	(1.4)	1.2	-	-	(1.9)	1.6
Net book value	**38.9**	**13.8**	**162.2**	**123.1**	**29.4**	**29.6**	**230.5**	**166.5**

5.3 Intangible assets

Goodwill

All business combinations are accounted for by applying the acquisition method. Goodwill represents the difference between the cost of the acquisition and the fair value of the net identifiable assets acquired.

Goodwill is stated at cost less any accumulated impairment losses. Goodwill is tested annually for impairment.

IT system costs

IT system costs are recognised as an intangible asset where Cochlear controls future economic benefits as a result of the costs incurred, and are stated at cost less accumulated amortisation. Costs include expenditure directly related to the development and implementation (hardware and software costs) of IT systems including direct labour.

Other intangible assets

Other intangible assets, comprising acquired technology, patents and licences, customer relationships, capitalised development expenditure and intellectual property, are acquired individually or through business combinations and are stated at cost less accumulated amortisation and impairment losses (see below).

Amortisation

Amortisation is calculated to expense the cost of intangible assets less their estimated residual values on a straight-line basis over their estimated useful lives. The estimated useful lives for the current and comparative years are as follows: IT system costs between two to seven years, acquired technology, patents and licences between four to 15 years, customer relationships up to 31 years and capitalised development expenditure between four to 10 years.

Amortisation is recognised in the income statement from the date the assets are available for use unless their lives are indefinite.

Goodwill and intangible assets with an indefinite useful life are systematically tested for impairment annually.

	Intangible assets with indefinite useful life	Intangible assets with finite useful life			Intangible assets
	Goodwill	IT system costs	Acquired technology, patents and licences	Other intangible assets	Total
	$m	$m	$m	$m	$m
2020					
At cost	270.9	127.4	127.4	55.4	581.1
Accumulated amortisation and impairment losses	-	(69.3)	(73.8)	(27.7)	(170.8)
Net book value	**270.9**	**58.1**	**53.6**	**27.7**	**410.3**
Reconciliations of the carrying amounts are:					
Opening balance	268.8	50.4	72.5	32.7	424.4
Additions	-	18.5	4.4	-	22.9
Amortisation	-	(10.8)	(6.6)	(5.1)	(22.5)
Impairment	-	-	(16.7)	-	(16.7)
Effect of movements in foreign exchange	2.1	-	-	0.1	2.2
Net book value	**270.9**	**58.1**	**53.6**	**27.7**	**410.3**
2019					
At cost	268.8	109.2	122.9	56.3	557.2
Accumulated amortisation	-	(58.8)	(50.4)	(23.6)	(132.8)
Net book value	**268.8**	**50.4**	**72.5**	**32.7**	**424.4**
Reconciliations of the carrying amounts are:					
Opening balance	265.4	32.9	29.0	18.0	345.3
Additions	-	26.7	48.4	15.3	90.4
Amortisation	-	(9.2)	(4.9)	(1.5)	(15.6)
Effect of movements in foreign exchange	3.4	-	-	0.9	4.3
Net book value	**268.8**	**50.4**	**72.5**	**32.7**	**424.4**

Impairment

Cochlear annually tests goodwill and other intangible assets with indefinite useful life for impairment. Other non-financial assets, other than inventories (see Note 5.1) and deferred tax assets (see Note 3.2), are tested if there is any indication of impairment or if there is any indication that an impairment loss recognised in a prior period may no longer exist or may have decreased.

Assets are impaired if their carrying value exceeds their recoverable amount. The asset's recoverable amount is estimated based on its value in use.

An asset that does not generate independent cash flows and its individual value in use cannot be estimated is tested for impairment as part of a cash generating unit (CGU).

An impairment loss is recognised in the income statement when the carrying amount of an asset or CGU exceeds its recoverable amount. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised. An impairment loss in respect of goodwill is not reversed.

Impairment tests for CGUs

Cochlear allocates goodwill and other intangible assets to CGUs based on the expected benefits that each CGU will receive from use of those assets.

The aggregate carrying amounts of goodwill allocated to each CGU are:

	Americas $m	EMEA $m	Asia Pacific $m	Total $m
2020	185.2	75.5	10.2	270.9
2019	184.2	74.6	10.0	268.8

The recoverable amount of each CGU is based on value-in-use calculations. Those calculations use five year cash flow projections based on actual operating results and recent experience and learnings in relation to the economic impacts of COVID-19 on Cochlear's business. The calculation contains increased estimation uncertainty from potential COVID-19 impacts which may include government restrictions on elective surgeries and demand impacts due to the broader economic environment.

The calculation assumes that the future economic impact of COVID-19 will primarily impact FY21 with gradually improving trading conditions. While uncertainty resulting from COVID-19 remains, Cochlear will continue to manage costs by limiting non-essential spending in each CGU. Future year forecasts include an EBIT growth rate, considered modest compared to historical growth rates in the CGUs.

Cash flows for year 6 onwards are extrapolated using a terminal growth rate of 3.0% (2019: 3.0%) per annum which is consistent with long-term growth rates. The pre-tax discount rate for each CGU is as follows: Americas 9.6% (2019: 10.6%), EMEA 9.8% (2019: 10.3%) and Asia Pacific 10.3% (2019: 11.2%).

The key assumptions and the approach to determining their value in the current year are:

Assumption	How determined
Discount rate	Based on weighted average cost of capital reflecting current market assessments of the time value of money and risks specific to the CGU.
EBIT growth rate	Based on a five year cash flow projection taking into account historical growth rates and product lifecycle.
Terminal value growth rate	Based on long-term growth rates.

The recoverable amount of each CGU including unallocated corporate assets is in excess of the carrying amount and therefore no impairment expense was recognised. The above represents the best estimate of the directors. Sensitivity analysis has been undertaken to stress test cash flow forecasts, discount rates and terminal value growth rate assumptions to reflect a prolonged recovery and growth rate. Based on the range and depth of sensitivities applied no reasonable change in assumptions would result in an impairment.

5.4 Investments

Cochlear's investments are valued individually using quoted prices or unobservable market inputs. 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. Refer to Note 6.4(d) for further details on the valuation of financial assets.

Equity investments at fair value through other comprehensive income are ordinary shares. Investments measured at fair value through profit or loss are interests in entities that do not meet the definition of equity, such as instruments convertible into ordinary shares.

	2020 $m	2019 $m
Opening balance	47.8	15.8
Additions	14.2	22.1
Fair value gain through profit or loss	35.8	10.8
Fair value loss through other comprehensive income	(1.8)	(1.3)
Transferred to equity accounted investments	(70.2)	-
Effect of movements in foreign exchange	0.1	0.4
Total investments	**25.9**	**47.8**

At 30 June 2020, $22.7 million of investments is measured at fair valued through profit or loss with the remaining $3.2 million measured at fair valued through other comprehensive income.

5.5 Equity accounted investments

In February 2020, Cochlear executed an agreement to invest an additional EUR 8.0 million in Nyxoah S.A. The additional investment resulted in Cochlear's ownership interest exceeding 20% and the investee has been reclassified as an associate from February 2020.

Associates are accounted for using the equity method with Cochlear recognising its share of the associate's profit or loss and other comprehensive income. Transactions with associates are eliminated to the extent of Cochlear's interest in the associate until such time as they are realised by the investee on consumption or sale. Investments in associates are assessed for impairment when indicators of impairment are present and if required, written down to the recoverable amount.

If Cochlear's share of losses exceeds its interest in the associate, the carrying amount is reduced to nil and recognition of further losses is discontinued except to the extent that Cochlear has incurred legal or constructive obligations or made payments on behalf of the associate.

In the current year, Cochlear has recognised $1.2 million in losses representing its proportionate share of Nyxoah S.A.'s net loss since it became an equity accounted investment. At 30 June 2020, the value of this investment is $69.0 million.

5.6 Provisions

A provision is recognised in the balance sheet when:

- Cochlear has a present obligation (legal or constructive) as a result of a past event;
- a reliable estimate can be made of the amount of the obligation; and
- it is probable that an outflow of economic benefits will be required to settle the obligation.

Provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and the risk specific to the liability.

2020	Warranties $m	Legal and insurance $m	Product recall $m	Make good lease costs $m	Total $m
Opening balance	37.8	22.0	10.5	1.2	71.5
Provision made	4.6	97.5	-	0.4	102.5
Provision used	(11.4)	(4.3)	(1.5)	-	(17.2)
Effect of movements in foreign exchange	0.6	-	-	-	0.6
Total provisions	**31.6**	**115.2**	**9.0**	**1.6**	**157.4**
Represented by:					
Current	13.6	115.2	1.4	-	130.2
Non-current	18.0	-	7.6	1.6	27.2
Total provisions	**31.6**	**115.2**	**9.0**	**1.6**	**157.4**

Warranties

A provision for warranty claims is recognised in relation to sales made prior to the reporting date, based on historical claim rates and respective product populations. Warranty periods on hardware products extend for three to 10 years.

Legal and insurance

Cochlear is involved in litigation in the ordinary course of business, including claims made by Cochlear and against Cochlear for patent infringement. Where Cochlear is able to make a reliable estimate of the estimated future costs related to these proceeding, including legal fees, a provision is recognised.

The legal and insurance provision also includes amounts provided in relation to the long-running patent dispute with Alfred E. Mann Foundation for Scientific Research and Advanced Bionics LLC (collectively referred to as AMF and AB). The increased provision relates primarily to the additional USD 75 million provided in relation to the claims by AMF and AB for pre-judgment interest and attorneys' fees. Refer to Note 2.3 for further details.

Cochlear self-insures certain risks associated with operating in its line of business. Claims are recognised when an incident occurs that may give rise to a claim. They are measured at the cost that Cochlear expects to incur in defending or settling the claims, discounted using a rate that reflects current market assessments of the time value of money and the risks specific to the liability.

Product recall

On 11 September 2011, the Company initiated a worldwide voluntary recall of its unimplanted Nucleus CI500 cochlear implant range. Management has made judgements, estimates and assumptions related to probable costs arising from the recall which affect the reported amounts of assets, liabilities, income and expenses. Actual outcomes may differ from these estimates as further information is identified.

No additional provisions have been made or released to the income statement for the year ended 30 June 2020.

Make good lease costs

Cochlear has a number of operating leases over its offices that require the premises to be returned to the lessor in their original condition. The operating lease payments do not include an element for the repairs and overhauls.

5.7 Contingent liabilities

The details of contingent liabilities are set out 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.

Regulatory actions

Cochlear operates in multiple overseas jurisdictions and is currently, and/or is likely from time to time to be, subject to tax, customs and regulatory reviews, audits and investigations. Known reviews, audits and investigations are not expected to result in a significant adverse outcome for Cochlear. Outcomes are uncertain because investigations are ongoing.

5.8 Leases

Cochlear leases a number of assets including land and buildings, office equipment and motor vehicles. Cochlear's lease agreements often include a standard lease term with an extension option at the end. Lease agreements may include annual rent increases based on either a fixed percentage or benchmarked against an inflation index. Land and building leases may also include periodic market rent reviews which resets the rent to the market rent at the time of the review.

At inception of a contract, Cochlear assesses whether a contract is, or contains, a lease. A contract is, or contains, a lease, if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration.

Where the contract contains a lease, a lease liability is recognised at lease commencement date. The liability is initially measured at the present value of future lease payments, discounted using Cochlear's incremental borrowing rate.

The lease liability is subsequently remeasured when there is a modification in future lease payments arising from a change in an index or rate, a change in the estimate of the amount expected to be payable under a residual value guarantee, or changes in the assessment of whether a purchase or extension option is reasonably certain to be exercised or a termination option is reasonably certain not to be exercised. The right of use asset is initially measured at cost and subsequently adjusted for certain remeasurements of the lease liability.

Over the life of the lease, the lease liability will be increased by interest costs and will be reduced as lease payments are made. The right of use asset is amortised on a straight-line basis over its useful life. As compared to AASB 117 Leases, the pattern of expense recognition changes with a higher expense at lease commencement due to a higher lease liability at that time.

Under AASB 117, operating lease payments are expensed on a straight-line basis over the term of the lease, except where an alternatives basis is more representative of the pattern of benefits to be derived from the leased property. Minimum lease payments include fixed rate increases.

Cochlear has applied judgement to determine the lease term for some lease contracts in which it is a lessee that include renewal options. The assessment of whether Cochlear is reasonably certain to exercise such options impacts the lease term, which significantly affects the amount of lease liabilities and right of use assets recognised.

Cochlear has elected not to recognise a right of use asset and a corresponding lease liability for leases with a term of less than 12 months or for leases of low-value assets. Cochlear recognises the lease payments associated with these leases as an expense on a straight-line basis over the lease term.

The following table shows movements in the right of use asset during the year:

	Land and buildings $m	Other assets $m	Total $m
Balance at 1 July 2019	171.4	6.8	**178.2**
Depreciation expense	(24.0)	(4.4)	**(28.4)**
Additions to right of use asset	54.6	3.9	**58.5**
Total right of use asset	**202.0**	**6.3**	**208.3**

Cochlear recognised $28.4 million in depreciation expense and $6.1 million in interest expense instead of the operating lease expense recognised under the previous standard.

The operating lease expense under AASB 117 and the right of use asset depreciation under AASB 16 are both recognised in cost of sales, selling, marketing and general expenses, research and development expenses and administration expenses in the income statement depending on the function of associated activities. Interest expense incurred on the lease liability under AASB 16 is recognised in finance expense – interest in the income statement.

For the purpose of presentation of the statement of cash flows, the lease payments under AASB 16 are separated into principal payments (financing activities) of $24.6 million and interest payments (operating activities) of $6.1 million. Under AASB 117, lease payments are included in cash paid to suppliers and employees in the statement of cash flows.

Transition to AASB 16

Cochlear has initially adopted AASB 16 Leases from 1 July 2019, this has replaced AASB 117. Cochlear adopted AASB 16 using the modified retrospective approach. Under this approach, the cumulative impact of adoption was recognised as an adjustment to opening retained earnings with no restatement of comparative periods.

Under AASB 117, Cochlear classified leases as either operating leases or finance leases based on its assessment of whether the lease transferred substantially all the risks and rewards of ownership. Under AASB 16, Cochlear recognises a right of use asset and a corresponding lease liability for most leases i.e. these leases are on balance sheet.

Lease liabilities were measured at the present value of the remaining lease payments at 1 July 2019, discounted at Cochlear's incremental borrowing rate as at 1 July 2019. Right of use assets were measured at their carrying amount as if AASB 16 had been applied since the commencement date, discounted using Cochlear's incremental borrowing rate at the date of initial application.

Cochlear has elected to apply practical expedients allowed under the modified retrospective approach not to recognise right of use assets or lease liabilities for leases with less than 12 months of lease term remaining at the transition date or leases of low-value assets.

The adoption of AASB 16, as outlined above, resulted in the following change in the balance sheet on 1 July 2019:

	Total $m
Increase in right of use assets	178.2
Increase in deferred tax assets	5.6
Increase in lease liabilities (current and non-current)	(197.8)
Decrease in other liabilities	1.9
Decrease in retained earnings	12.1

The following table reconciles the differences between the non-cancellable lease commitments as disclosed in the FY19 Annual Financial Statements under AASB 117 and the lease liability recognised on transition to AASB 16:

	$m
Operating lease commitments disclosed at 30 June 2019	220.8
Add: Adjustments as a result of different treatment of extension options	112.5
Less: Lease executed but not yet effective on transition date	(84.5)
Less: Other	(7.8)
Discounted using incremental borrowing rate at the date of initial application	(43.2)
Lease liability recognised as at 1 July 2019	**197.8**

Lease terms range from one to 25 years. The weighted average incremental borrowing rate applied is 3.0% per annum.

6. Capital and financial structure

6.1 Capital management

Cochlear's capital management objectives are to safeguard its ability to continue as a going concern, provide returns to shareholders, provide benefits to other stakeholders and maintain an optimal capital structure to reduce the cost of capital.

The Board aims to maintain and develop a capital base appropriate to Cochlear's objectives and monitors a number of qualitative metrics as follows:

- net gearing ratio – defined as net debt as a proportion of net debt plus total equity;
- dividend payout ratio – defined as dividends as a proportion of net profit after tax for a given period;
- growth in EPS – defined as the compound annual growth percentage in EPS over a three year period; and
- TSR – defined as the percentage growth in share price over a three year period plus the cumulative three year dividend return calculated against the opening share price in the same three year period.

Senior management tracks, manages and reports against these capital management metrics periodically as part of broader corporate governance responsibilities. The Board undertakes periodic reviews to assess whether the metrics continue to be appropriate and whether the capital management structure is appropriate to meet Cochlear's medium and long-term strategic requirements.

In order to maintain or adjust the capital structure, Cochlear may adjust the amount of dividends paid to shareholders, return capital to shareholders, issue new shares or sell assets to reduce debt. Neither the Company nor any of its subsidiaries is subject to externally imposed capital requirements.

In the year ended 30 June 2020 and in response to the combined effects of COVID-19 and the patent litigation, Cochlear increased its liquidity by taking the following steps:

- a capital raising of AUD 1,075.6 million (net of related costs). The capital raising was to ensure Cochlear remained strongly capitalised during the market uncertainties of COVID-19 and to position Cochlear for the future;
- increase total available debt from AUD 414.5 million in 2019 to AUD 1,003.8 million. Additional facilities were obtained from existing lenders of AUD 225.0 million for working capital and USD 268 million for the patent litigation;
- obtaining covenant waivers from all Cochlear's lenders for the leverage and interest cover ratio covenants testing periods June 2020 and December 2020; and
- determined that no final 2020 dividend will be paid.

Cochlear's priorities for the use of cash from the capital raising and the availability of the new debt facilities is to strengthen the balance sheet to support the business during the impacts of COVID-19 while continuing to invest in core strategic business priorities and research and development, to respond to the patent litigation expense and to reduce existing net debt levels. At the appropriate time, Cochlear will resume the dividend to shareholders.

As a result of the capital raising, Cochlear is now in a net cash rather than a net debt position for the year ended 30 June 2020.

Cochlear's net gearing ratio was as follows:

	Note	2020 $m	2019 $m
Net (cash)/debt	6.3(a)	(457.0)	103.0
Total equity - reported		1,401.5	725.9
Net gearing ratio at 30 June		**(48%)**[1]	**12%**

1. Net gearing ratio is negative due to net cash in 2020.

6.2 Capital and reserves

Share capital

The Company does not have authorised capital or par value in respect of its issued shares.

	Total number of issued shares	
	2020	**2019**
On issue 1 July – fully paid	**57,715,821**	**57,547,820**
Issued for nil consideration under Employee Share Plan	7,955	7,590
Issued from exercise of APAC Equity Plan	826	1,092
Issued from the exercise of options	54,419	112,093
Issued from the exercise of performance rights	51,099	47,226
Issued from capital raising – institutional placement	6,285,715	-
Issued from capital raising – share purchase plan	1,571,567	-
On issue 30 June – fully paid	**65,687,402**	**57,715,821**

During the 2020 financial year, Cochlear purchased 10,394 shares (2019: 18,813 shares) on market to satisfy exercise of options and performance rights.

Cochlear has also issued shares to employees under the Employee Share Plan (see Note 4.3).

Ordinary shares are classified as equity and incremental costs directly attributable to the issue of ordinary shares and share options are recognised as a deduction from equity, net of any income tax benefit.

The holders of ordinary shares are entitled to receive dividends as declared from time to time and are entitled to one vote per share at shareholders' meetings.

In response to the combined effects of COVID-19 and the patent litigation, Cochlear adjusted its capital structure by a capital raising of AUD 1,075.6 million, net of related costs. The capital raising was to ensure Cochlear remained strongly capitalised during the market uncertainties of COVID-19, enhance Cochlear's balance sheet and to strengthen liquidity in order to position Cochlear for the future.

From the capital raise, 6,285,715 shares were issued from the institutional placement on 31 March 2020 and 1,571,567 shares were issued from the share purchase plan on 30 April 2020.

Translation reserve

The translation reserve records the foreign currency differences arising from the translation of the financial statements of foreign operations as well as from the translation of liabilities that hedge the Company's net investment in a foreign subsidiary, where their functional currency is different to the presentation currency of the reporting entity. See Note 1.2(e) for further details.

Hedging reserve

The hedging reserve comprises the effective portion of the cumulative net change in the fair value of cash flow hedging instruments related to underlying transactions that have not yet occurred.

Fair value reserve

The fair value reserve comprises the cumulative net change in the fair value of investments revalued through other comprehensive income until the assets are derecognised or impaired.

Share based payment reserve

The share based payment reserve comprises the cost of shares, options, performance shares and performance rights granted to eligible executives under the CEIP, as detailed in Note 4.3 less any payments made to meet Cochlear's obligations through the acquisition of shares on market, together with any deferred tax asset/liability on such payments.

6.3 Net debt and finance costs

(a) Net debt

Loans and borrowings are recognised initially at fair value less attributable transaction costs. Subsequently, loans and borrowings are stated at amortised cost, with any difference between amortised cost and redemption value being recognised in the income statement over the period of the borrowings on an effective interest rate basis.

Debt establishment costs are capitalised and recognised as a reduction in loans and borrowings. They are recorded initially at cost and are amortised over the period of the loan. Included within loans and borrowings is an amount of $0.9 million (2019: $0.8 million) in relation to unamortised loan establishment fees.

	2020 $m	2019 $m
Loans and borrowings		
Current	393.1	3.3
Non-current	79.9	178.3
Total loans and borrowings	**473.0**	**181.6**
Less: Cash and cash equivalents	(565.0)	(78.6)
Less: Term deposits	(365.0)	-
Net (cash)/debt	**(457.0)**	**103.0**

(b) Term deposits

Term deposits are bank deposits with a fixed term maturity of longer than three months from inception. Bank deposits with a fixed term of less than 3 months are classified as cash and cash equivalents. All term deposits held at 30 June 2020 will mature by January 2021. Term deposits of AUD 365.0 million (2019: AUD nil) were held as at 30 June 2020.

(c) Financing arrangements

	Multi-option bank facilities		Other credit facilities		
	Unsecured bank loan $m	Bank guarantees[2] $m	Unsecured bank overdrafts $m	Unsecured bank loan $m	Bank guarantees[2] $m
2020					
Utilised at reporting date[1]	470.5	8.0	-	3.4	5.4
Not utilised at reporting date	527.2	7.0	2.9	2.7	4.2
Total facilities	**997.7**	**15.0**	**2.9**	**6.1**	**9.6**
2019					
Utilised at reporting date[1]	179.1	5.3	-	3.3	4.6
Not utilised at reporting date	229.4	9.7	2.9	2.7	5.1
Total facilities	**408.5**	**15.0**	**2.9**	**6.0**	**9.7**

1. Excludes the amount of $0.9 million (2019: $0.8 million) in relation to unamortised loan establishment fees.
2. Bank guarantees include standby letters of credit.

Multi-option bank facilities - Unsecured bank loan

During the year ended 30 June 2020, Cochlear restructured its bank loan facilities as follows:

Facility type	<1 year term $m	1 - 2 year term $m	2 - 3 year term $m	3 - 4 year term $m	Total facilities $m
Committed debt including guarantees	389.8	325.0	146.7	151.2	1,012.7

All facilities are unsecured and have interlocking guarantees provided by certain controlled entities. Interest on the facilities is variable and charged 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.

Unsecured bank loan

Cochlear has a USD 268.0 million loan facility, a Japanese yen (JPY) 450.0 million loan facility, a Swedish kroner (SEK) 300.0 million loan facility and a Chinese yuan (CNY) 176.0 million loan facility. The facilities are unsecured bank loans. Interest on unsecured bank loans is variable and is charged at prevailing market rates.

Bank guarantees/Standby letters of credit

As at 30 June 2020, Cochlear had additional contingent liability facilities denominated in USD, Euros (EUR), Sterling (GBP), Indian rupees and New Zealand dollars totalling AUD 9.6 million (2019: AUD 9.7 million).

(d) Finance costs

Interest income is recognised as it accrues in the income statement. Borrowing costs are recognised as they accrue in the income statement as a finance expense.

6.4 Financial risk management

The activities of Cochlear are exposed to a variety of risks, including market risk (comprising currency and interest rate risk), credit risk and liquidity risk. Cochlear’s overall risk management program considers the unpredictability of financial markets and seeks to appropriately manage the potential adverse effects on financial performance.

The Board has overall responsibility for the establishment and oversight of the Risk Management Framework. Under instruction of the Board, management has established a Risk Management Committee which is responsible for identifying, assessing and appropriately managing risk throughout Cochlear. Key risks are reported to the Audit & Risk Committee on a regular basis.

The Audit & Risk Committee oversees how management monitors compliance with Cochlear’s Risk Management Framework, policies and procedures and is assisted by Group Risk and Assurance which undertakes reviews of key management controls and procedures.

(a) Market risk

Market risk is the risk that changes in market prices, such as foreign exchange rates, interest rates and equity prices, will affect Cochlear’s net profit or the value of its holdings of financial instruments.

The objective of market risk management is to manage and control market risk exposures by buying and selling forward exchange contracts and incurring financial liabilities, within acceptable parameters, while optimising the return, all in accordance with the treasury risk policy.

Currency risk

Cochlear is exposed to currencies other than the respective functional currencies of the controlled entities, primarily AUD, Swiss francs (CHF), CNY, EUR, GBP, JPY, SEK and USD.

Over 90% of Cochlear's revenues and over 50% of costs are denominated in currencies other than AUD. Currency risk is hedged in accordance with the treasury risk policy. Risk resulting from the translation of assets and liabilities of foreign operations into Cochlear's reporting currency is not hedged.

Cochlear's exposure to foreign currency risk in relation to non-derivative financial instruments at 30 June 2020 was as follows, based upon notional amounts:

Amounts local currency/millions	CHF	CNY	EUR	GBP	JPY	SEK	USD
2020							
Trade receivables	0.6	6.0	36.5	(0.9)	771.8	1.7	66.4
Unsecured bank loan	-	(165.4)	-	-	(250.0)	(300.0)	(268.0)
Trade payables	(0.1)	(26.3)	(10.6)	(3.0)	(74.4)	(39.9)	(23.8)
Balance sheet exposure	**0.5**	**(185.7)**	**25.9**	**(3.9)**	**447.4**	**(338.2)**	**(225.4)**
2019							
Trade receivables	0.5	12.2	59.4	5.7	1,139.7	7.5	78.0
Unsecured bank loan	-	(14.1)	-	-	(250.0)	(300.0)	-
Trade payables	(0.9)	(20.8)	(8.4)	(4.8)	(122.1)	(44.2)	(17.4)
Balance sheet exposure	**(0.4)**	**(22.7)**	**51.0**	**0.9**	**767.6**	**(336.7)**	**60.6**

Derivative assets and liabilities

In order to reduce the impact of short-term fluctuations on Cochlear's earnings, Cochlear enters into forward exchange contracts to hedge anticipated sales and purchases in CHF, EUR, GBP, JPY, SEK and USD. The amounts of forward cover taken are in accordance with approved policy and internal forecasts.

In the year ended 30 June 2020, Cochlear designated the majority of forward exchange contracts as cash flow hedges. These are hedges of forecast future transactions to manage the currency risk arising from exchange rate fluctuations. The hedged items were highly probable foreign currency transactions.

At the start of a hedge relationship, Cochlear designates and documents the relationship between the hedging instrument and hedged item. This includes identification of the hedging instrument, the hedged item or transaction, the nature of the risk being hedged and how Cochlear will assess the effectiveness of the hedging relationship. Cochlear regularly assesses whether the hedging instruments are expected to be highly effective in offsetting the changes in the cash flows of the respective hedged items.

Forward exchange contracts are recognised initially at fair value. Subsequently, forward exchange contracts are measured at fair value. Changes in the fair value are recognised directly in equity to the extent that the hedge is effective. The ineffective part of any hedging instrument is recognised immediately in the income statement.

If the forward exchange contract no longer meets the criteria for hedge accounting, expires or is sold, terminated or exercised, then hedge accounting is discontinued prospectively. The cumulative gain or loss previously recognised in equity remains there until the forecast transaction occurs or when cash flows arising from the transaction are received.

For cash flow hedges, the associated cumulative gain or loss is removed from equity and recognised in the income statement in the same period the hedged forecast transaction affects the income statement and on the same line item as that hedged forecast transaction.

In the year ended 30 June 2020, Cochlear assessed that its forward exchange contracts to hedge sales revenues in EUR, GBP and USD for periods less than one year were no longer highly effective due to the combined effects of COVID-19 and the patent litigation on the probable foreign currency cash flows anticipated to be received during that period. As a result, those cash flow hedges no longer met the criteria for hedge accounting and hedge accounting on those cash flow hedges was discontinued. The associated cumulative gain/(loss) was removed from equity and recognised in the income statement in the same period that hedge accounting was discontinued. In addition, the ineffective forward exchange contracts were terminated with a total loss of AUD 26.1 million (2019: AUD nil).

All other cash flow hedges with terms greater than 1 year were effective at the reporting date and continue to meet the criteria for hedge accounting.

The following table sets out the gross value to be received or paid under remaining forward exchange contracts and the weighted average contracted exchange rates of outstanding contracts:

	Weighted average rate	< 1 year $m	1 - 2 years $m	2 - 5 years $m
2020				
Buy CHF	0.659	(12.0)	-	-
Sell EUR	0.595	-	63.1	-
Sell GBP	0.522	-	9.6	-
Sell JPY	72.979	19.8	11.1	-
Buy SEK	6.492	(27.7)	-	-
Sell USD	0.691	-	122.8	26.3
Total		**(19.9)**	**206.6**	**26.3**
2019				
Buy CHF	0.697	(19.9)	-	-
Sell EUR	0.606	141.2	84.7	7.6
Sell GBP	0.541	20.2	14.9	1.9
Sell JPY	76.902	17.7	9.5	1.6
Buy SEK	6.391	(43.0)	-	-
Sell USD	0.746	266.0	135.0	21.0
Total		**382.2**	**244.1**	**32.1**

Currency risk - Sensitivity analysis

An analysis based on a 10% strengthening of foreign currencies would have increased Cochlear's loss for the year ended 30 June 2020 after tax by approximately AUD 1.7 million (2019: decrease profit by AUD 2.5 million) and increased Cochlear's equity by AUD 13.6 million (2019: increase by AUD 25.8 million). A 10% weakening of the foreign currencies would have decreased Cochlear's loss after tax by AUD 2.4 million (2019: increased profit by AUD 3.5 million) and decreased equity by AUD 13.0 million (2019: decrease by AUD 67.2 million).

This analysis assumes that all other variables remain constant and ignores any impact from the translation of foreign operations.

The following significant exchange rates applied to Cochlear during the year:

	Average rate		Reporting date spot rate	
AUD 1 =	**2020**	**2019**	**2020**	**2019**
CHF	0.656	0.712	0.654	0.683
CNY	4.725	4.877	4.869	4.814
EUR	0.606	0.627	0.611	0.616
GBP	0.533	0.553	0.558	0.552
JPY	72.549	79.582	73.985	75.355
SEK	6.457	6.557	6.413	6.494
USD	0.672	0.716	0.688	0.700

Interest rate risk

Cochlear is exposed to interest rate risks in Australia, China, Japan and Sweden. See Note 6.4(c) for effective interest rates, repayment and repricing analysis of outstanding debt.

In order to reduce the impact of fluctuations in market interest rates, Cochlear had previously entered into interest rate swaps to manage the interest rate risk by using a floating versus fixed rate debt framework. The notional principal amount of these interest rate swaps was $50.0 million. These interest rate swaps were closed out in May 2020.

At the reporting date, the interest rate profile of Cochlear's interest-bearing financial instruments is financial assets of $930.0 million (2019: $78.6 million) and financial liabilities of $473.0 million (2019: $181.6 million).

Interest rate risk - Sensitivity analysis

For the year ended 30 June 2020, it is estimated that a general increase of one percent in interest rates would have increased Cochlear's loss after income tax and equity by approximately $3.3 million (2019: decrease profit by $0.7 million). A one percent general decrease in interest rates would have had the equal but opposite effect on Cochlear's loss and equity.

(b) Credit risk

Credit risk is the risk of financial loss to Cochlear if a customer or counterparty to a financial instrument fails to meet its contractual obligations. Cochlear is exposed to credit risk from its operating activities (primarily from trade and other receivables) and from financing activities, including deposits with financial institutions and foreign exchange contracts. The carrying amounts of these financial assets at year end represent Cochlear's maximum exposure to credit risk.

Credit risk management - Trade and other receivables

Customer credit risk is managed at a regional level, subject to Board approved policies and procedures. The ageing profile of total receivables balances, individually significant debtors by geographic region, high risk customers and collection activities are reported to management and the Board on a monthly basis. Where high risk customers are identified, regional management is responsible for placing restrictions on future trading, including suspending future shipments and administering dispatches on a prepayment basis.

Cochlear's exposure to credit risk is influenced mainly by the political and geographical location and characteristics of individual customers. Cochlear does not have a significant concentration of credit risk with a single customer.

The maximum exposure to credit risk for trade receivables at the reporting date by geographic region was:

	Americas $m	EMEA $m	Asia Pacific $m	Total $m
2020	74.7	92.1	44.6	**211.4**
2019	96.0	140.1	63.4	**299.5**

Depending on the region, Cochlear's credit terms are generally 30 days; however, there are certain jurisdictions where it is customary practice for customers to make payment beyond 270 days. Although Cochlear discloses the balance as overdue, it is not indicative of a higher than normal credit risk as payments are typically received by Cochlear within the extended timeframes.

Cochlear has established an allowance for impairment that represents its estimate of the expected credit losses in respect of trade receivables. The expected credit losses are assessed by reference to historical collection trends and timing of recoveries of each customer type within a region.

In response to COVID-19, Cochlear undertook a review of its outstanding trade debtors at 30 June 2020. The review considered the macroeconomic conditions and outlook in the country that the customer is located as well as any specific collection risk identified by either Cochlear or the customer. As a result of this review, the trade debtors provision has been increased to reflect these higher levels of risks caused by COVID-19. While these model inputs including forward looking information was revised, the expected credit loss model remains consistent with the prior year.

Trade and other receivables are stated at amortised cost less impairment losses. The ageing of Cochlear's trade receivables at the reporting date was:

	2020 $m	2019 $m
Trade receivables		
Not past due	163.5	239.3
Past due 1 - 60 days	31.6	42.4
Past due 61 - 180 days	19.8	16.7
Past due 181 - 360 days	11.6	6.6
Past due 361 days and over	8.8	8.4
	235.3	**313.4**
Allowance for impairment losses	(23.9)	(13.9)
Trade receivables net of allowance for impairment losses	**211.4**	**299.5**
Other receivables - current	24.1	20.2
Trade and other receivables	**235.5**	**319.7**

Credit risk management - Cash deposits, term deposits and forward exchange contracts

The majority of Cochlear's cash deposits, term deposits and all forward exchange contracts are only executed with leading financial institutions whose credit rating is at least A on the Standard & Poor's rating index.

(c) Liquidity risk

Liquidity risk is the risk that Cochlear will not be able to meet its financial obligations as they fall due. Cochlear manages liquidity risk by ensuring, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due. The capital raising of AUD 1,075.6 million net of related costs and extra debt facilities, increased Cochlear's liquidity such that Cochlear is now in a net cash position for the year ended 30 June 2020 (refer Note 6.1). This has ensured that Cochlear has a strengthened balance sheet and is well positioned to meet all liabilities when due.

Non-derivative liabilities

Contractual maturities of non-derivative financial liabilities, including estimated interest payments and excluding the impact of netting agreements, are as follows:

	Effective interest rate Per annum	Carrying amount $m	Contractual cash flows $m	< 1 year $m	1 - 2 years $m	2 - 5 years $m	More than 5 years $m
2020							
USD floating rate loan	1.17%	389.8	394.3	394.3	-	-	-
CNY floating rate loan	2.60%	34.0	37.6	0.9	0.9	35.8	-
JPY floating rate loan	0.55%	3.3	3.4	3.4	-	-	-
SEK floating rate loan	0.91%	45.9	47.8	0.2	0.4	47.2	-
Trade and other payables	-	172.9	172.9	159.3	12.4	1.2	-
Lease liability	-	231.5	282.6	26.0	28.2	77.7	150.7
Total		**877.4**	**938.6**	**584.1**	**41.9**	**161.9**	**150.7**
2019							
AUD floating rate loan	2.42%	129.2	138.0	3.1	63.1	71.8	-
CNY floating rate loan	4.11%	2.9	3.5	0.1	0.1	3.3	-
JPY floating rate loan	0.53%	3.3	3.3	3.3	-	-	-
SEK floating rate loan	0.57%	46.2	46.5	0.3	46.2	-	-
Trade and other payables	-	203.2	203.2	160.8	30.3	12.1	-
Total		**384.8**	**394.5**	**167.6**	**139.7**	**87.2**	**-**

It is not expected that the cash flows included in the maturity analysis could occur significantly earlier or at significantly different amounts.

Derivative assets and liabilities

The following table indicates the periods in which the cash flows associated with Cochlear's derivatives are expected to occur:

	Carrying amount $m	Contractual cash flows $m	< 1 year $m	1 - 2 years $m	2 - 5 years $m
2020					
Assets	3.3	3.3	1.2	2.0	0.1
Liabilities	(2.0)	(2.0)	(0.3)	(1.6)	(0.1)
Total	**1.3**	**1.3**	**0.9**	**0.4**	**-**
2019					
Assets	4.3	4.4	2.2	2.1	0.1
Liabilities	(28.5)	(27.7)	(22.6)	(5.0)	(0.1)
Total	**(24.2)**	**(23.3)**	**(20.4)**	**(2.9)**	**-**

The expected impact on the income statement is not considered to be significantly different to the cash flow impact noted above.

(d) Fair value

The carrying amounts and estimated fair values 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 year.

7. Other notes

7.1 Auditors' remuneration

	2020 $	2019 $
Audit services		
Auditors of the Company - KPMG:		
- audit and review of financial reports	2,170,767	1,809,019
Total audit services	**2,170,767**	**1,809,019**
Non-audit services		
Auditors of the Company - KPMG:		
- other assurance services	35,666	133,481
- taxation compliance and advisory services	1,547,505	1,764,533
- IT advisory	-	643,260
- other	9,185	357,650
Total non-audit services	**1,592,356**	**2,898,924**

7.2 Commitments

Capital expenditure commitments

As at 30 June 2020, Cochlear entered into contracts to purchase property, plant and equipment for $24.0 million (2019: $44.0 million).

7.3 Controlled entities

Subsidiaries conduct business transactions with various controlled entities. Such transactions include purchases and sales of certain products, dividends, interest and loans.

	Interest held		Country of incorporation/formation
	2020 %	2019 %	
Company			
Cochlear Limited			Australia
Controlled entities			
Cochlear AG	100	100	Switzerland
Cochlear Americas	100	100	USA
Cochlear Austria GmbH	100	100	Austria
Cochlear Benelux NV	100	100	Belgium
Cochlear Bone Anchored Solutions AB	100	100	Sweden
Cochlear Boulder LLC	100	100	USA
Cochlear Canada Inc	100	100	Canada
Cochlear Clinical Services LLC	100	100	USA
Cochlear Colombia SAS	100	100	Colombia
Cochlear Deutschland GmbH & Co KG	100	100	Germany
Cochlear Employee Share Trust	100	100	Australia
Cochlear Europe Finance GmbH	100	100	Germany
Cochlear Europe Limited	100	100	UK
Cochlear Finance Pty Limited	100	100	Australia

Cochlear France SAS		100	100	France
Cochlear German Holdings Pty Limited		100	100	Australia
Cochlear Incentive Plan Pty Ltd		100	100	Australia
Cochlear Investments Pty Ltd		100	100	Australia
Cochlear Investments (No. 2) Pty Ltd		100	100	Australia
Cochlear Italia SRL		100	100	Italy
Cochlear Korea Limited		100	100	Korea
Cochlear Labs Pty Limited		100	100	Australia
Cochlear Latinoamerica S.A.		100	100	Panama
Cochlear Malaysia Sdn. Bhd.		100	100	Malaysia
Cochlear Manufacturing Corporation		100	100	USA
Cochlear Medical Device (Beijing) Co., Ltd		100	100	China
Cochlear Medical Device (Chengdu) Co Ltd		100	100	China
Cochlear Medical Device Company India Private Limited		100	100	India
Cochlear Mexico SA de CV		100	100	Mexico
Cochlear Middle East FZ-LLC		100	100	UAE
Cochlear Nordic AB		100	100	Sweden
Cochlear Norway AS		100	100	Norway
Cochlear NZ Limited		100	100	New Zealand
Cochlear Research and Development Limited		100	100	UK
Cochlear Shared Services S.A.		100	100	Panama
Cochlear Sweden Holdings AB		100	100	Sweden
Cochlear Taiwan Limited	(i)	100	-	Taiwan
Cochlear Thailand Limited		100	100	Thailand
Cochlear Tibbi Cihazlar ve Saglik Hizmetleri Limited Sirketi		100	100	Turkey
Cochlear Verwaltungs GmbH		100	100	Germany
Cochlear (HK) Limited		100	100	Hong Kong
Cochlear (UK) Limited	(ii)	100	100	UK
Medical Insurance Pte Limited		100	100	Singapore
Nihon Cochlear Co Limited		100	100	Japan
Sichuan Keli ShuangChuang Technology Co Ltd		51	51	China
Sycle, LLC		100	100	USA
Sycle.Net Technologies (Canada) Ltd		100	100	Canada

(i) Incorporated in November 2019.
(ii) Dormant.

7.4 Parent entity disclosure

At, and throughout the financial year ended, 30 June 2020, the parent company of Cochlear was Cochlear Limited.

	2020 $m	2019 $m
Result of the parent entity		
Net (loss)/profit	(191.4)	225.0
Other comprehensive income/(loss)	17.9	(4.0)
Total comprehensive (loss)/income	**(173.5)**	**221.0**
Financial position of the parent entity at year end		
Current assets	1,441.8	456.0
Total assets	**2,154.8**	**1,015.7**
Current liabilities	689.0	211.7
Total liabilities	**922.0**	**502.4**

	2020 $m	2019 $m
Total equity of the parent entity comprising:		
Share capital	1,272.4	182.3
Hedging reserve	0.9	(17.0)
Share based payment reserve	58.0	50.0
(Accumulated losses)/retained earnings	(98.5)	298.0
Total equity	**1,232.8**	**513.3**

Dividend income from subsidiaries is recognised by the parent entity when the dividends are declared by the subsidiary.

Parent entity contingencies

The details of all contingent liabilities in respect to Cochlear Limited are disclosed in Note 5.7.

Parent entity capital commitments for acquisition of plant and equipment

As at 30 June 2020, the parent entity entered into contracts but had not provided for or paid to purchase plant and equipment for $10.1 million (2019: $17.0 million).

7.5 Deed of Cross Guarantee

Cochlear Limited (the holding entity) together with wholly owned subsidiaries set out below (together referred to as the 'Closed Group') have entered a Deed of Cross Guarantee on 17 April 2019 in accordance with ASIC Corporations (Wholly-owned Companies) Instrument 2016/785 and are relieved from the *Corporations Act 2001* requirement to prepare and lodge an audited financial report and directors' report. The effect of the deed is that Cochlear Limited has guaranteed to pay any outstanding liabilities upon the winding up of any wholly owned subsidiary that is party to the Deed. Wholly owned subsidiaries that are party to the Deed have also been given a similar guarantee in the event that Cochlear Limited or another party to the Deed is wound up.

The subsidiaries party to the deed are:
Cochlear Finance Pty Limited;
Cochlear German Holdings Pty Limited;
Cochlear Investments Pty Ltd;
Cochlear Investments (No. 2) Pty Ltd; and
Cochlear Labs Pty Limited.

Set out below is the income statement, statement of comprehensive income, a summary of movements in (accumulated losses)/retained earnings and balance sheet of the entities party to the Deed of Cross Guarantee for the year ended 30 June 2020 and 30 June 2019:

	2020 $m	2019 $m
Income statement		
Revenue	851.1	972.9
Cost of sales	(307.2)	(310.4)
Gross profit	**543.9**	**662.5**
Selling, marketing and general expenses	(63.3)	(65.4)
Research and development expenses	(141.8)	(122.6)
Administration expenses	(88.3)	(92.8)
Other income	178.8	34.3
Other expenses	(107.7)	(102.6)
Patent litigation expense	(503.7)	-
Share of losses on equity accounted investments	(1.2)	-
Results from operating activities	**(183.3)**	**313.4**
Finance income - interest	3.0	10.7
Finance expense - interest	(10.0)	(16.6)
Net finance expense	**(7.0)**	**(5.9)**
(Loss)/profit before income tax	**(190.3)**	**307.5**
Income tax benefit/(expense)	37.1	(81.3)
Net (loss)/profit	**(153.2)**	**226.2**
Statement of comprehensive income		
Financial investments measured at fair value through other comprehensive income, net of tax	(1.8)	(1.3)
Foreign currency translation differences	(2.2)	18.7
Effective portion of changes in fair value of cash flow hedges, net of tax	(22.6)	(17.8)
Net change in fair value of discontinued cash flow hedges transferred to the income statement, net of tax	18.3	-
Net change in fair value of cash flow hedges transferred to the income statement, net of tax	22.3	13.6
Total comprehensive (loss)/income	**(139.2)**	**239.4**
Retained earnings at beginning of year	275.0	232.3
Transfers to and from reserves	(166.1)	224.5
Dividends recognised	(193.7)	(181.8)
(Accumulated losses)/retained earnings at end of year	**(84.8)**	**275.0**

Balance sheet	2020 $m	2019 $m
Assets		
Cash and cash equivalents	432.9	21.8
Term deposits	365.0	-
Trade and other receivables	443.2	306.6
Forward exchange contracts	1.0	2.0
Inventories	137.6	111.9
Current tax assets	53.5	5.0
Prepayments	9.4	14.4
Total current assets	**1,442.6**	**461.7**
Other receivables	5.0	3.1
Forward exchange contracts	2.1	2.1
Loans and borrowings - internal	79.8	60.0
Investments in subsidiaries	441.1	462.6
Equity accounted investments	69.0	-
Property, plant and equipment	109.4	110.6
Intangible assets	107.4	121.3
Deferred tax assets	90.1	42.8
Right of use asset	117.6	-
Total non-current assets	**1,021.5**	**802.5**
Total assets	**2,464.1**	**1,264.2**
Liabilities		
Trade and other payables	115.0	114.7
Forward exchange contracts	0.3	20.9
Loans and borrowings - external	389.8	-
Loans and borrowings - internal	74.5	60.5
Current tax liabilities	1.7	23.2
Employee benefit liabilities	32.6	38.7
Provisions	139.6	17.0
Deferred revenue	2.6	2.3
Lease liability	13.4	-
Total current liabilities	**769.5**	**277.3**
Trade and other payables	51.3	81.8
Forward exchange contracts	1.7	7.6
Loans and borrowings - external	45.9	175.4
Loans and borrowings - internal	208.4	188.2
Employee benefit liabilities	4.7	4.7
Provisions	5.5	40.3
Deferred tax liabilities	12.9	4.6
Deferred revenue	2.0	-
Lease liability	123.8	-
Total non-current liabilities	**456.2**	**502.6**
Total liabilities	**1,225.7**	**779.9**
Net assets	**1,238.4**	**484.3**
Equity		
Share capital	1,272.4	182.3
Reserves	50.8	27.0
(Accumulated losses)/retained earnings	(84.8)	275.0
Total equity	**1,238.4**	**484.3**

7.6 Changes in accounting policies

Cochlear has adopted AASB 16 Leases from 1 July 2019. Due to the transition methods chosen, comparative information throughout these financial statements has not been restated to reflect the requirements of the new standards.

Refer to Note 5.8 for further details on the accounting for leases under AASB 16 and the transition impacts.

7.7 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 2020 and have not been applied in preparing these consolidated financial statements. These new standards, amendments and interpretations are not expected to have an effect on the consolidated financial statements of Cochlear.

7.8 Events subsequent to the reporting date

Other than the patent litigation detailed in Note 2.3, 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 significantly affect the operations of Cochlear, the results of those operations, or the state of affairs of Cochlear in future financial years.

Directors' declaration

1. In the opinion of the directors of Cochlear Limited (the Company):
   a) the consolidated financial statements and notes and the Remuneration report are in accordance with the *Corporations Act 2001*, including:
      i) giving a true and fair view of the Consolidated Entity's financial position as at 30 June 2020 and of its performance for the financial year ended on that date; and
      ii) complying with Australian Accounting Standards and the *Corporations Regulations 2001*; and
   b) there are reasonable grounds to believe that the Company will be able to pay its debts as and when they become due and payable; and
   c) at the date of this declaration, there are reasonable grounds to believe that the Company and each of the Closed Group entities identified in Note 7.5 will be able to meet any liabilities to which they are or may become subject to, because of the Deed of Cross Guarantee between the Company and those group entities pursuant to ASIC Corporations (Wholly-owned Companies) Instrument 2016/785.
2. The directors have been given the declarations required by section 295A of the *Corporations Act 2001* from the Chief Executive Officer & President and Chief Financial Officer for the financial year ended 30 June 2020.
3. The directors draw attention to Note 1.2(a) to the consolidated financial statements, which includes a statement of compliance with International Financial Reporting Standards.

Signed in accordance with a resolution of the directors:

Dated at Sydney this 18th day of August 2020.

Director

Director

Independent audit report to the shareholders of Cochlear Limited

Report on the audit of the Financial Report

Opinion

We have audited the Financial Report of Cochlear Limited (the Company).

In our opinion, the accompanying Financial Report of the Company is in accordance with the *Corporations Act 2001*, including:

- giving a true and fair view of the Consolidated Entity's financial position as at 30 June 2020 and of its financial performance for the year ended on that date; and
- complying with Australian Accounting Standards and the *Corporations Regulations 2001*.

The Financial Report comprises:

- Balance sheet as at 30 June 2020;
- Income statement, Statement of comprehensive income, Statement of changes in equity, and Statement of cash flows for the year then ended;
- Notes including a summary of significant accounting policies; and
- Directors' Declaration.

The Consolidated Entity consists of the Company and the entities it controlled at the year-end or from time to time during the financial year.

Basis for opinion

We conducted our audit in accordance with Australian Auditing Standards. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Our responsibilities under those standards are further described in the Auditor's responsibilities for the audit of the Financial Report section of our report.

We are independent of the Consolidated Entity in accordance with the *Corporations Act 2001* and the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 Code of Ethics for Professional Accountants (the Code) that are relevant to our audit of the Financial Report in Australia. We have fulfilled our other ethical responsibilities in accordance with the Code.

Key Audit Matters

The key audit matters we identified are:

- Recoverability of trade receivables; and
- Warranty provision.

Key Audit Matters are those matters that, in our professional judgement, were of most significance in our audit of the Financial Report of the current period.

These matters were addressed in the context of our audit of the Financial Report as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Recoverability of trade receivables $211.4 million

Refer to Note 6.4(b) Financial risk management, credit risk

The key audit matter	How the matter was addressed in our audit
Recoverability of trade receivables was considered a key audit matter due to: • The varying characteristics of customers which include governments, government-supported universities, clinics and major hospital chains; • The different geographical locations of customers and the political and economic environments they are	Our procedures included: • With the assistance of our IT specialists, testing key controls within the credit control process including: - management review and approval of new customer credit limits within the Consolidated Entity's credit limit policies; - the system configuration of credit limits; and

subject to, which may affect the timely recovery of certain receivables; • Trade receivables past due at the reporting date which have certain risk characteristics and therefore have a greater inherent risk of not being recovered; • The potential for COVID-19 to increase the risk of receivables being delayed for a prolonged period or not paid; • The inherent subjectivity involved in the Consolidated Entity making forward-looking judgements in relation to the recovery of credit risk exposures; and • The Consolidated Entity's adoption of AASB 9 Financial Instruments requiring the use of an expected credit loss model. These conditions gave rise to additional audit effort, including: • Greater involvement by our senior team members to gather evidence across the various customer profiles and their trade receivables; and • To challenge the forward-looking judgements made by the Consolidated Entity. We involved IT specialists to supplement our senior team members in assessing this key audit matter.	- management's evaluation of trade receivables ageing and trade receivables past due; • Assessing the Consolidated Entity's expected credit loss model in significant geographies against the requirements of the accounting standards; • Challenging the Consolidated Entity's view of credit risk and recoverability in certain locations by selecting a sample of significant overdue customer balances with indicators of credit deterioration. We: - noted the historical patterns for long outstanding trade receivables in those locations for those customer types, to form an understanding of the normal pattern of recovery and compared this to the age of the customer balances sampled; - assessed cash received subsequent to year-end from the Consolidated Entity's bank statements for its effect in reducing amounts outstanding at year-end; - evaluated other evidence including customer correspondence; - questioned the Consolidated Entity's assessment of the impact of Covid-19 on the risk of default; and - questioned the Consolidated Entity's knowledge of future conditions which may impact expected customer receipts based on consistency with the results of the procedures performed above; and • Assessing the Consolidated Entity's disclosures of the quantitative and qualitative considerations in relation to trade receivable credit risk, by comparing these disclosures to our understanding of the matter and the requirements of the accounting standards.

Warranty provision $31.6 million

Refer to Note 5.6 Provisions

The key audit matter	How the matter was addressed in our audit
The warranty provision was considered a key audit matter due to: • The estimation uncertainty inherent in the key assumptions applied by the Consolidated Entity to determine the warranty provision; • The Consolidated Entity's evolving product portfolio, through the introduction of new generations, where	Our procedures included: • Obtaining an understanding of the evolving product portfolio, each product's warrantable period and history of claim rates, and the different attributes which impact the key assumptions used in the Consolidated Entity's warranty provision; • Testing the sensitivity of the warranty provision by varying key assumptions, within a reasonably possible range, to focus our further procedures;

each product's design and quality attributes can impact the key assumptions;

- The increased use of the Global Repair Centre intended to reduce forecast repair cost;
- The inherent unpredictability of future failures resulting in claims under warranty; and
- The calculation is largely manually developed and therefore is at greater risk of error.

The key assumptions used in the Consolidated Entity's determination of the warranty provision are:

- The forecast claim rates of the multiple products in the portfolio;
- The ratio of repairing to replacing failed products;
- The forecast repair cost; and
- The forecast replacement cost which is based on standard forecasts of manufacturing costs.

Challenging these key assumptions required greater involvement by our senior team members.

- Challenging the Consolidated Entity's ability to reliably estimate the key assumptions by comparing previous estimates to actual outcomes;
- Assessing the integrity of the model for the warranty provision. This included checking the accuracy of the formulas within the model;
- Comparing the forecast claim rates of a sample of products to the historical warranty claims for that product or the historical warranty claims of previous generations of similar products;
- Comparing the forecast proportion of claims that can be repaired and associated repair costs to historical performance of the Global Repair Centre;
- Comparing the forecast replacement cost to:
  - the standard manufacturing cost used in board approved budgets; and
  - actual manufacturing costs to identify variances and their impact on the warranty provision;
- Enquiring of management responsible for product design and quality attributes and the Global Repair Centre to challenge the forward-looking assumptions used in the model; and
- Assessing the disclosures of the quantitative and qualitative considerations in relation to the warranty provision, by comparing these disclosures to our understanding of the matter and the requirements of the accounting standards.

Other Information

Other Information is financial and non-financial information in Cochlear Limited's annual reporting which is provided in addition to the Financial Report and the Auditor's Report. The Directors are responsible for the Other Information.

Our opinion on the Financial Report does not cover the Other Information and, accordingly, we do not express an audit opinion or any form of assurance conclusion thereon, with the exception of the Remuneration Report and our related assurance opinion.

In connection with our audit of the Financial Report, our responsibility is to read the Other Information. In doing so, we consider whether the Other Information is materially inconsistent with the Financial Report or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

We are required to report if we conclude that there is a material misstatement of this Other Information, and based on the work we have performed on the Other Information that we obtained prior to the date of this Auditor's Report we have nothing to report.

KPMG

Independent auditor's report to the shareholders of Cochlear Limited

Responsibilities of the Directors for the Financial Report

The Directors are responsible for:

- preparing the Financial Report that gives a true and fair view in accordance with Australian Accounting Standards and the *Corporations Act 2001*; and
- implementing necessary internal controls to enable the preparation of a Financial Report that gives a true and fair view and is free from material misstatement, whether due to fraud or error; and
- assessing the Consolidated Entity's ability to continue as a going concern and whether the use of the going concern basis of accounting is appropriate. This includes disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless they either intend to liquidate the Consolidated Entity or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities for the audit of the Financial Report

Our objective is:

- to obtain reasonable assurance about whether the Financial Report as a whole is free from material misstatement, whether due to fraud or error; and
- to issue an Auditor's Report that includes our opinion.

Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Australian Auditing Standards will always detect a material misstatement when it exists.

Misstatements can arise from fraud or error. They are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the Financial Report.

A further description of our responsibilities for the audit of the Financial Report is located at the Auditing and Assurance Standards Board website at: http://www.auasb.gov.au/auditors_responsibilities/ar1.pdf. This description forms part of our Auditor's Report.

Report on the Remuneration Report

Opinion

In our opinion, the Remuneration Report of Cochlear Limited for the year ended 30 June 2020, complies with Section 300A of the *Corporations Act 2001*.

Directors' responsibilities

The Directors of the Company are responsible for the preparation and presentation of the Remuneration Report in accordance with Section 300A of the *Corporations Act 2001*.

Our responsibilities

We have audited the Remuneration Report included in pages 40 to 57 of the Directors' report for the year ended 30 June 2020.

Our responsibility is to express an opinion on the Remuneration Report, based on our audit conducted in accordance with Australian Auditing Standards.

KPMG

KPMG
Sydney, 18 August 2020

Julian McPherson, Partner

References

Market leadership

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23. World Alzheimer Report 2015 (https://www.alz.co.uk/research/WorldAlzheimerReport2015.pdf).
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Shareholder information

Additional information required by Australian Securities Exchange Listing Rules and not disclosed elsewhere in this report – the information presented is as at 31 July 2020.

Substantial shareholders

Investor	Number of ordinary shares	%
Baillie Gifford & Co	3,944,356	6.0
BlackRock Inc	3,930,851	6.0
Veritas Asset Mgt	3,696,542	5.6
The Vanguard Group, Inc	3,602,454	5.5
Total	**15,174,203**	**23.1**

Distribution of shareholders

Number of shares held	Number of ordinary shareholders	% shares
1 - 1,000	39,479	10.9
1,001 - 5,000	2,828	8.2
5,001 - 10,000	132	1.3
10,001 - 100,000	78	2.9
100,001 and over	14	76.7
Total	**42,531**	**100.0**

Non-marketable parcels – 129 shareholders held less than a marketable parcel of ordinary shares.

Twenty largest shareholders

Shareholder	Number of ordinary shares	%
HSBC Custody Nominees (Australia) Limited	28,405,386	43.24
J P Morgan Nominees Australia Pty Limited	11,371,030	17.31
Citicorp Nominees Pty Limited	4,113,509	6.26
National Nominees Limited	1,682,907	2.56
BNP Paribas Noms Pty Ltd <DRP>	1,540,107	2.34
BNP Paribas Nominees Pty Ltd <Agency Lending DRP A/C>	1,132,094	1.72
HSBC Custody Nominees (Australia) Limited-GSCO ECA	738,643	1.12
Australian Foundation Investment Company Limited	323,715	0.49
HSBC Custody Nominees (Australia) Limited <NT-Comnwlth Super CORP A/C>	300,693	0.46
Netwealth Investments Limited <Wrap Services A/C>	231,860	0.35
Citicorp Nominees Pty Limited <Colonial First State INV A/C>	226,944	0.35
Mr Christopher Graham Roberts	162,173	0.25
BNP Paribas Nominees Pty Ltd Hub24 Custodial Serv Ltd <DRP A/C>	103,774	0.16
PGA (Investments) Pty Ltd	100,118	0.15
National Nominees Limited <DB A/C>	86,230	0.13
AMP Life Limited	79,421	0.12
HSBC Custody Nominees (Australia) Limited - A/C 2	71,519	0.11
UBS Nominees Pty Ltd	70,592	0.11
Avanteos Investments Limited <Encircle IMA A/C>	68,964	0.10
Custodial Services Limited <Beneficiaries Holding A/C>	67,214	0.10
	50,876,893	**77.43**

The 20 largest shareholders held 77.43% of the ordinary shares of the Company.

On market buy-back

There is no current on market buy-back.

Contact information

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Shareholder enquiries

Access to shareholding information is available to investors through Computershare.

Computershare Investor Services Pty Limited

GPO Box 2975

Melbourne VIC 3001

Australia

Telephone: 1300 850 505

Email: web.queries@computershare.com.au

Website: www.computershare.com.au

Calendar of events

18 August 2020	FY20 results announced
8 September 2020	Closing date for receipt of director nominations
20 October 2020	Annual general meeting
19 February 2021	HY21 results announced*
20 August 2021	FY21 results announced*

* Indicative dates only.

Annual general meeting

The annual general meeting (AGM) of Cochlear Limited will be held on 20 October 2020 at 10.00am as a virtual meeting. Shareholders will be advised of further details regarding the 2020 AGM in a separate Notice of Meeting, which will be provided to shareholders in mid-September 2020. The Notice of Meeting will also be available on the ASX Company Announcements Platform and Cochlear's website at www.cochlear.com.

Hear now. And always

As the global leader in implantable hearing solutions, Cochlear is dedicated to helping people with moderate to profound hearing loss experience a life full of hearing. We have provided more than 600,000 implantable devices, helping people of all ages to hear and connect with life's opportunities.

We aim to give people the best lifelong hearing experience and access to innovative future technologies. We have the industry's best clinical, research and support networks.

That's why more people choose Cochlear than any other hearing implant company.

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www.cochlear.com

Please seek advice from your health professional about treatments for hearing loss. Outcomes may vary, and your health professional will advise you about the factors which could affect your outcome. Always read the instructions for use. Not all products are available in all countries. Please contact your local Cochlear representative for product information.

Views expressed are those of the individual. Consult your health professional to determine if you are a candidate for Cochlear technology.

The Cochlear Nucleus Smart App is available on App Store and Google Play. The Cochlear Nucleus 7 Sound Processor is compatible with Apple and Android devices, for compatibility information visit www.cochlear.com/compatibility.