

Media Release

Phonak Holding AG

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Subject	2003/04 Financial Results
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2003/04: Record Level of Sales, EBITA and Net Income

Increased Dividend Payment to CHF 0.20 per Share

The Management of the Phonak Group is pleased to report the results for the 2003/04 financial year, in which the Group achieved a record level of sales, operating profit (EBITA) and net income. Sales reached CHF 637.6 million, which represents an increase of 15.8% in reported currency. In local currency, the growth over last year was 18.8%. Operating profit (EBITA) amounted to CHF 103.3 million, which is more than double the prior year! Net profit was CHF 68.9 million, which yields an earnings per share of CHF 1.06.

These results stem primarily from internal improvements that have led to a significant number of successful product launches. The Group now benefits from having a complete digital product portfolio – from the high-end to the low-end – under both the Phonak and the Unitron Hearing brands. The Group also continues to benefit from its innovative wireless communication products.

During 2004/05, management believes that the Group will benefit from the sales of products launched in 2003/04 as well as the new sales opportunities that will arise from products launched in 2004/05 as well as expansions in the distribution network.

At the General Meeting, shareholders will be asked to approve a dividend payment of CHF 0.20 per share.

Overview of operating performance

Sales of premium hearing instruments, including *Perseo*, *Claro* and *Liaison*, grew significantly over the prior year and accounted for 31% (previous year 25%) of total sales in 2003/04. The success of *Perseo* explains the majority of the increase in sales above the original guidance for the year of CHF 600 million.

Mid-level hearing instruments, including Phonak's *Supero* and *Aero* as well as Unitron Hearing's *Conversa*, accounted for 24% of total sales (previous year 28%). In addition, sales of *Supero +*, the world's first digital line specifically designed to meet the needs of severe to profound hearing impaired people, developed well.

Sales of hearing instruments in the economy segment also grew significantly over the prior year due to the success of *MAXX*, Phonak's first digital offering in this class, as well as *Unison*, Unitron Hearing's entry level digital product line, which was launched two years ago and continues to sell well. These sales accounted for 25% of total sales (previous year 25%).

Sales of wireless FM systems grew over the previous year due mainly to the success of the new MLx synthesized receiver. Sales of all FM systems and remote controls accounted for 7% of total sales (previous year 7%).

Gross profit reached CHF 367.7 million, or 57.7% of sales, compared to 279.1 million, or 50.7% of sales, in the prior year. As announced at the beginning of last fiscal year, gross margin was expected to improve as a result of an improved product mix, coming from an expanded product portfolio, the launch of several premium and mid-level digital products, and the transition from analog product sales to digital product sales in the low-end product segment. The strong sales of *Perseo* throughout the entire fiscal year have led to an increase in gross margin greater than expected.

Operating profit before goodwill amortization (EBITA) increased to CHF 103.3 million, which is a record level, and 114.5% above last year's result. EBITA is now 16.2% of sales, compared to only 8.7% of sales in the prior year.

Research and development spending increased, as expected, in 2003/04 to CHF 58.2 million or 9.1% of total sales. The increase was due to the timing of major development projects, especially of *Palio*, the development of a new product hardware platform, which was nearing completion by the end of the fiscal period.

Sales and marketing costs were CHF 126.1 million, up CHF 10 million from the previous year. As a percentage of sales, however, sales and marketing spending has fallen to 19.8% (previous year 21.1%) given that a certain portion of these costs are fixed and do not vary with the sales result.

Administration and general overhead costs, combined with other expenses (net), were CHF 78.2 million and up from the previous year, due to the strengthening of the Group's management team, the investment in IT infrastructure and systems, as well as the investments in creating the Chinese manufacturing facility and the Japanese sales company.

The operating profit after goodwill amortization (EBIT) was CHF 94.7 million, compared to CHF 37.6 million in the prior year (before the one-time impairment charge).

Consolidated net income was CHF 68.9 million, compared to a net loss of CHF 46.9 million in the prior year. Before the one-time impairment charge, the prior year result was a net income of CHF 28.1 million.

Many new products launched in 2003/04

Many new products were again launched in 2003/04. Combined with the new products launched in 2002/03, there have been eight entire new product families launched and several extensions to existing product families. Sales of products launched in the past 24 months account for 58% of the Group's total sales in 2003/04.

In addition to the launch of Phonak's new premium product line *Perseo* in March 2003, the following is a summary of the key product launches during the past fiscal year:

- *MAXX* and *Amio*, Phonak's new entry level digital products, launched in June 2003;
- *Conversa*, Unitron Hearing's mid-level digital product line launched in June 2003;
- *Supero +*, an enhanced version of Phonak's digital high power line, launched in October 2003;
- *MAXX directional*, which adds directional signal processing to the entry-level product family, launched in October 2003; and
- *Liaison*, Unitron Hearing's new high-end product line, launched in October 2003.

Within the FM business segment, the Group continued to leverage existing key technology into new applications. With *SmartLink*, Phonak has achieved another industry first by allowing hearing instrument users to access other communications systems. *SmartLink* combines a remote control, a transmitter, a directional microphone system and a Bluetooth link to mobile

phone all in one single device. Phonak also presented *EduLink*, an innovative FM device to assist the learning development of children with Auditory Processing Disorder (APD). *EduLink* was perceived very positively within the medical community and recent classroom tests show favourable results.

More new products launched in 2004/05

As a stated objective, the Group will continue to set the pace for innovative product development in the industry. Already in the first quarter of 2004/05, the Phonak Group has launched the following new products:

- *Valeo*, Phonak's new digital product line in the mid-level segment;
- *PowerMAXX*, an extension to the popular *MAXX* entry-level product line by Phonak, which is the world's most powerful miniature digital hearing instrument; and
- *Unison Plus*, Unitron Hearing's new entry level digital line, expanding on the success of *Unison*.

Finally, throughout 2004/05, more new products will be launched, including another premium high-end digital product which will be based on the new Palio hardware platform.

New market development

During 2003/04, management has worked closely with the major key accounts and retail chains to secure an increasing share of their business with Phonak and Unitron Hearing products. In addition, work is underway to expand the Group's distribution network. During 2003/04, the Group opened its own distribution company in Japan, entered into a distribution agreement with Japan's market leader, Rion, strengthened its retail position in Austria, through the acquisition of Viennatone, opened a sales office in India to begin to develop this market over the longterm, and opened Unitron Hearing sales offices in the United Kingdom and France. Also, as announced in February 2004, the Group acquired the former Phonak and Unitron Hearing agents in China and will use these organizations as a basis for establishing both a wholesale and a retail sales organization in China. In 2004/05, the Group will work on developing its sales network in Eastern Europe and in South America.

Outlook

The management of the Phonak Group is confident that sales will continue to develop positively based on products launched in 2003/04 as well as the new sales opportunities that will arise from products launched in 2004/05 and the recent expansions made in the distribution network. Based on today's perspective and on achieving product launch deadlines, the sales target for 2004/05 is CHF 700 million, which represents a 10% growth in reported currency.

Phonak Group expects a further net improvement in the gross profit percentage in 2004/05 compared to the result in 2003/04. On the one hand, gross profit percentage improvement will come from the impact of Chinese manufacturing and the launch at the end of 2004 of the first Palio-based product.

Following the peak of spending in research and development in 2003/04, spending in 2004/05 will be around 7% of sales. In absolute terms, of course, the company retains a high level of spending in research and development.

Management also expects further improvements in the EBITA margin as a result of the expected gross profit improvements as well as the planned research and development spending, both in absolute amount and as a percentage of sales. If the expected gross profit improvements are achieved, the Group will reach the upper range of its previously stated mid-term EBITA target of 15–20%.

Capital expenditures will increase slightly over the level in 2003/04. Major projects include tooling for new products (housings of new products introduced on Palio platform), IT infrastructure and SAP project implementation and production equipment.

Investor Relations Calendar

July 8, 2004, 3 p.m.	Annual General Meeting of Phonak Holding AG (at the Congress Hall in Zurich)
November 2004	Semi-annual Report per September 30, 2004
June 7, 2005	Media Conference/Analyst Meeting; Mailing of Annual Report 2004/05
July 7, 2005	Annual General Meeting of Phonak Holding AG

Key Figures

	2003/04 (CHF m)	2002/03 (CHF m)	Change over previous year
Consolidated sales	638	550	+15.8%
Operating income (EBITA)	103	48	+114.5%
<i>as % of consolidated sales</i>	16.2	8.7	
Operating income/loss (EBIT) – as reported ¹⁾	95	-37	+353.5%
<i>as % of consolidated sales</i>	14.9	-6.8	
Consolidated net income/loss – as reported ¹⁾	69	-47	+246.9%
<i>as % of consolidated sales</i>	10.8	-8.5	
Cash flow from operating activities	146	49	+196.5%
Research and development	58	49	+19.1%
<i>as % of consolidated sales</i>	9.1	8.9	
Capital expenditure	21	22	
Total assets	684	607	+12.7%
Shareholders' equity	349	290	+20.6%
<i>as % of total assets</i>	51.0	47.7	
Number of employees (March 31, 2004)	2,689	2,385	+12.7%
Earnings per share in CHF – as reported ¹⁾	1.056	-0.721	+246.9%
Dividend per share in CHF	0.20 ²⁾	0.12	

¹⁾ After one-time impairment charge of CHF 75 m in the previous year.

²⁾ Proposal to the General Meeting of July 8, 2004.