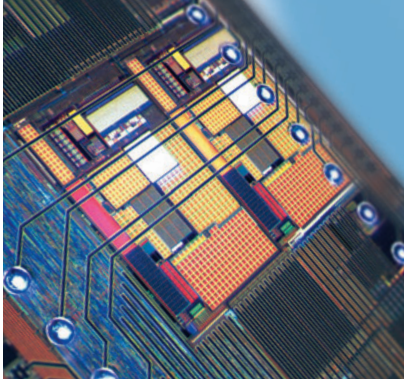
Semi-Annual Report per September 30, 2004



The Art and Science of Better Hearing

PHONAK
hearing systems

Dear Phonak Shareholder

We are pleased to present the half year results of the Phonak Group for the 2004/05 fiscal year.
The Group has achieved an 8% year-over-year growth (representing 10% growth in local currency), an improved gross margin, and an improved EBITA margin.

In the first half of the year – which is historically weaker than the second half because it includes the summer holiday months – sales reached CHF 325 million. This represents a 10% growth, in local currencies, over the same period last year, and was driven by consistent sales of Perseo, supported by strong growth in economy-level digital products as well as Phonak's FM products. The gross margin continued to increase over last year's first half result and the EBITA margin improved to 17%, compared to 13% for the same period last year.

While we continue to ramp up production in our new Chinese manufacturing facility, we have also opened our new sales facility in China in the first half year, beginning with the acquisitions of the former Phonak and Unitron Hearing distributors in China. Also in the first half of this year, we have made further developments in the Group's senior management team. With the appointment of Paul Thompson to Executive Vice President, Corporate Development, and the arrival of Oliver Walker as the new CFO, the Group has increased its senior management capacity and resources, which will be applied to opening new markets. Sarah Kreienbuehl has also joined the Phonak Group as Vice President of Corporate Human Resources, who will assist the Group in developing consistent, state-of-the-art processes to attract, retain and develop our most valuable resources.

Last month, the Phonak Group received a lot of attention and positive market feedback at the European trade show in Frankfurt. Phonak launched the next innovation in hearing technology – the new high-end product called Savia. It is the first hearing system ever to implement the unique capabilities of biological hearing systems using digital technology. In this way, we can finally provide the end user with a substantial improvement in hearing performance through the application of the most advanced signal processing running on a state-of-the-art chip set. Savia innovations like Real Ear Sound, digital SurroundZoom and Echo Block have become the new benchmarks in our industry. We have included a number of industry-first features that will benefit the audiologist and dispenser in selling and fitting this product to their patients. Starting in December, Savia will be introduced step by step until full global coverage in February. Unitron Hearing launched Unison 6, 3 and Essential, an expansion of its popular Unison line of digital products, as well as the WiFi mic, a dedicated CROS/BiCROS hearing system, while Phonak launched its universal CROSLink system.

As we continue on our path to bring the Phonak Group into a solid leadership position in this industry, we again want to thank our employees and partners for their great efforts and to our shareholders for their interest and support.

Andy Rihs	Dr. Valentin Chapero Rueda
Chairman of the Board	CEO

Business Report

Sales increase 10% over prior year

Sales in the first half year reached CHF 325 million, which is in line with our target growth, in local currency, of 10% over the same period last year. In reported currency, sales increased 8%, which is slightly negatively impacted by the translation of U.S. sales.

From a product perspective, while Perseo volume increased compared to the previous year, the major sales growth came from the economy-level product families, MAXX and Amio. In the mid-level segment, sales growth came from the new products, Valeo by Phonak and Conversa from Unitron Hearing. As expected with the launch of many new products, we saw sales of older products, such as Claro, Aero and analog economy-level products, decrease year-over-year. The Group's wireless FM products performed very well, driven particularly by the success of the MicroLink synthesized FM receiver launched last year, which has now been well adopted as the new industry standard.

Phonak Group:
Key figures for the six months ended September 30, 2004

	April to September 2004	2003	Change 6 months
	(CHF in millions)		2004/2003
Sales	325.0	300.9	+8.0%
Gross profit	193.5	164.8	+17.4%
% of sales	59.5	54.8	
Operating profit EBITA	56.0	39.1	+43.2%
% of sales	17.2	13.0	
Operating profit EBIT	56.0	34.9	+60.5%
% of sales	17.2	11.6	
Income after taxes	41.2	25.8	+59.7%
% of sales	12.7	8.6	
Net cash from operating activities	48.0	65.1	-26.3%
% of sales	14.8	21.6	
Capital expenditure	10.3	8.5	+21.2%
% of net cash from operating activities	21.4	13.1	
Total assets	698.9	630.4	+10.9%
Shareholders' equity	388.1	307.9	+26.1%
% of total assets	55.5	48.8	+6.7%
Net cash / (debt)	46.4	(49.7)	
Number of employees			
- At September 30	2'743	2,459	+11.5%
- Average	2'733	2,425	+12.7%

Interim financial statements are unaudited and are prepared
in accordance with International Financial Reporting Standards (IAS 34)

The product mix within hearing instruments remained stable compared to the prior year. Sales of premium hearing instruments still account for approximately 37% of total hearing instrument sales, while mid-level and economy-level account for 30% and 33% respectively.

Gross profit continues to improve

Gross profit for the first half year was CHF 193.5 million, which is a 17.4% increase over the gross profit of CHF 164.8 reported during the same period last year. As a percentage of sales, gross margin in the first half year was 59.5%, which is almost 500 basis points over the gross margin of 54.8% reported in the same period last year. This gross margin improvement came from efficiencies due to volume increases, savings in the purchase price of materials and the reduced manufacturing costs in China.

EBITA also continues to improve

Operating expenses, in total, were CHF 137.5 million which is 9.5% above the same period last year. Research and development expenses of CHF 26.5 million represent 8.1% of sales. During the same period last year, research and development spending was CHF 31.1 million or 10.3% of sales and, for the full year last year, the level was 9.1%. The reduction in spending, in relative terms, reflects the timing of expenses last year when costs for the Palio platform development reached their peak. Marketing and sales costs were CHF 73.5 million, which is 22.6% of sales and 20.8% above the same period last year. The increase reflects primarily the timing of Savia and other new product-related spending for launches in the second half of the year. Administration and general overhead costs were CHF 38.6 million, or 11.0% above the same period last year. This increase is due to the costs of the SAP world-wide implementation as well as the additional management resources in the Group.

EBITA in the first half was CHF 56.0 million, which is 43.0% higher than the level reported for the same period last year. This represents 17.2% of sales, compared to the 13.0% reported for 2003/04.

A strong balance sheet

Total assets as at September 30, 2004 increased to CHF 698.9 million, up 10.9% from September 30, 2003. The improvement in total assets is basically due to increased cash of CHF 57.1 million, mainly generated from operating activities. Trade receivables have remained consistent with the prior year, despite the sales increase, which demonstrates effective receivables management. Inventory increased slightly due to the pre-launch production activities for many new products. Taxes payable have increased due to the increased operating profit year over year. Trade payables and other liabilities and provisions have increased due to the increased business volume compared to the prior year. Long term debt has been reduced by CHF 36.6 million due to the regular debt repayments as well as the repayment of debt at higher interest rates.

Highlighting the strength of the balance sheet, the net cash position (cash and marketable securities of CHF 166.2 million less debt) was CHF 46.4 million, compared to a net debt position last year of CHF 49.7 million. In addition, the equity financing ratio (equity in % of total assets) has further increased to 55.5%, up from 48.8% last year.

A healthy cash flow

In the first half year, cash flow generated from operating activities was CHF 48.0 million.
Investing activities in the first half year, the majority of which are capital expenditures, required CHF 11.4 million, which is consistent with the prior year. In addition, CHF 24.3 million of cash was applied to debt repayment and CHF 13.1 million to shareholder dividends (67% increase from prior year). CHF 6.2 million was received due to the sale of treasury shares as well as the proceeds from shares issued under the stock option program.

New Management members

Joining the Group Executive Team in the first half year are **Oliver Walker** and **Sarah Kreienbuehl**. Effective October 1, 2004, Oliver Walker became the new CFO of the Group, replacing Paul Thompson who was appointed to the position of Executive Vice President, Corporate Development. At the beginning of August, Sarah Kreienbuehl joined as Vice President, Human Resources.

Outlook for the remainder of 2004/05

Based on current market conditions, and expecting a traditionally stronger second half year, combined with the first sales from the new premium product, Savia, we confirm our full year sales target of CHF 700 million, at constant currency rates. However, in the first half year, we have seen a negative 2% currency effect. Looking at the recent strengthening of the Swiss franc against the U.S. dollar, we estimate that sales in reported currency could be 2-3% less than CHF 700 million.

Due to higher expected sales volume in the second half, we forecast a slight improvement in gross profit margin and a slightly higher improvement in EBITA margin. The exact results will be dependant upon the Group's ability to meet the demand for Savia in the early months of launch.

Savia™
Digital Bionics

– the culmination of many key projects

The first shipments of Phonak's new high-end product, Savia, will begin in December.

This new product represents many accomplishments within the Phonak Group. First, Savia represents the next step in hearing instrument innovation, following the conversion to digital. Savia is the industry's first product ever to implement the unique capabilities of biological hearing systems using digital technology. Second, Savia is being launched on Phonak's new hardware platform, known as "Palio". This state-of-the-art, freely-programmable, powerful digital engine will provide the basic building block for the Group's product launches over the next 4 to 5 years. Third, Savia is presented in a totally new package – a new look and feel consistent with the features of this high-end product. Fourth, Savia will be sold and fit using iPFG, Phonak's new fitting software, developed on the "Chinook" fitting software architecture. This same fitting software architecture is the backbone also for the new Unitron Hearing fitting software, yet with a completely different graphical user interface.

These many key projects – Palio, Chinook, new product design, innovative product development – have come together in the development and launch of Savia. In the coming years, we expect to benefit in terms of product sales and reduced costs, from the building blocks we have developed over the past three years.

New: Perseo™ CIC Custom

is extremely precious, so is good hearing. Today, a satisfying hearing instrument needs to provide the perfection of natural sound and to capture this treasure in a form that is virtually invisible.

Hundreds of thousands of satisfied Perseo wearers around the world confirm that the latest Phonak hearing solutions have precious origins. These wearers appreciate the natural sound quality, excellent audibility and comfort that Perseo cutting-edge digital hearing technology brings, even in the most challenging hearing environments.

Consolidated Income Statement

April to September (1,000 CHF)

	Notes	2004	2003
Sales	3	325,032	300,919
Sales related costs		(12,424)	(13,784)
Cost of sales		(119,121)	(122,377)
Gross profit		193,487	164,758
Research and development		(26,467)	(31,076)
Marketing and sales		(73,489)	(60,834)
Administration and general overheads		(38,610)	(34,790)
Exchange differences		1,136	884
Other (expenses) / income, net		(78)	206
Operating profit (EBITA)		**55,979**	**39,148**
Goodwill amortization		0	(4,227)
Operating profit (EBIT)		55,979	34,921
Financial expense, net		(771)	(469)
Share of loss in associated company		(373)	(0)
Income before deduction of taxes and minority interests		54,835	34,452
Income taxes		(13,247)	(8,344)
Minority interest		(399)	(320)
Income after taxes		**41,189**	**25,788**
Basic earnings per share (CHF/share)			
before goodwill amortization	4	0.6297	0.4608
after goodwill amortization	4	0.6297	0.3960
Diluted earnings per share (CHF/share)			
before goodwill amortization	4	0.6224	0.4595
after goodwill amortization	4	0.6224	0.3948

Consolidated Balance Sheet

Assets

(1,000 CHF)	**30.09.2004**	**31.03.2004**	**30.09.2003**
Cash and cash equivalents	153,574	145,882	96,508
Short-term investments	12,675	11,417	10,022
Trade receivables	114,828	116,320	114,367
Other receivables and prepayments	23,177	16,285	15,248
Inventories	78,247	77,480	72,429
Total current assets	382,501	367,384	308,574
Land and buildings	65,295	66,475	66,920
Plant and equipment	58,190	58,926	58,057
Total tangible assets	**123,485**	**125,401**	**124,977**
Investments in associates	1,280	1,653	0
Other investments and long-term loans	10,422	10,127	10,056
Deferred tax assets	43,689	43,963	45,080
Intangible assets	132,655	131,562	136,917
Retirement benefit assets	4,843	4,115	4,817
Total non-current assets	316,374	316,821	321,847
Total assets	**698,875**	**684,205**	**630,421**

Liabilities and shareholders' equity

(1,000 CHF)	**30.09.2004**	**31.03.2004**	**30.09.2003**
Short-term debts	26,922	29,325	26,731
Trade payables	24,324	34,505	24,248
Taxes payable	23,116	17,341	14,817
Other liabilities and provisions	113,220	108,739	96,908
Total current liabilities	**187,582**	**189,910**	**162,704**
Mortgages	32,518	34,561	35,497
Other long-term debts	60,369	80,238	94,006
Deferred tax liabilities	17,633	17,944	19,401
Other liabilities and provisions	11,178	11,214	9,873
Total long-term liabilities	**121,698**	**143,957**	**158,777**
Total liabilities	309,280	333,867	321,481
Minority interests	1,502	1,248	1,086
Share capital	3,278	3,273	3,270
Capital reserves	138,230	135,164	134,351
Treasury shares	0	(3,960)	(3,961)
Retained earnings	266,305	238,190	195,097
Cumulative translation adjustment	(19,720)	(23,577)	(20,903)
Total shareholders' equity	388,093	349,090	307,854
Total liabilities and shareholders' equity	**698,875**	**684,205**	**630,421**

Condensed Consolidated Statement of Cash Flows

April to September (1,000 CHF)	Notes	2004	2003
Income after taxes		**41,189**	**25,788**
Minority interest in net income		399	320
Income tax expenses		13,247	8,344
Financial expenses, net		771	469
Share of loss in associated company		373	0
Operating profit (EBIT)		**55,979**	**34,921**
Depriciation of tangible assets		11,616	10,169
Amortization of intangible assets		0	4,623
Other non cash items		1,115	(131)
Cash flow before changes in working capital		**68,710**	**49,582**
Changes in net current assets		(11,229)	23,482
Cash generated from operations		**57,481**	**73,064**
Interest paid, net		(827)	(473)
Income taxes paid		(8,697)	(7,469)
Net cash from operating activities		**47,957**	**65,122**
Purchase of tangible assets		(10,253)	(8,522)
Proceeds from sale of tangible assets		353	184
Acquisition of subsidiaries (net of cash acquired)	2	(364)	0
Increase in other investments and loans		(1,171)	(3,876)
Net cash used in investing activities		**(11,435)**	**(12,214)**
Decrease in debts, net		(24,296)	(16,054)
Dividend paid by Phonak Holding AG		(13,074)	(7,811)
Other financial items, net		6,167	2,722
Proceeds from / (payments for) foreign exchange contracts		637	(5,767)
Net cash from financing activities		**(30,566)**	**(26,910)**
Currency translation differences		1,736	(4,518)
Increase in cash and cash equivalents		**7,692**	**21,480**
Cash and cash equivalents at April 1		145,882	75,028
Cash and cash equivalents at September 30		**153,574**	**96,508**

Summary of Changes in Shareholders' Equity

(1,000 CHF)	Share capital	Capital reserves	Retained earnings	Cumulative translation adjustment	Treasury shares	Total shareholders' equity
Balance April 1, 2003	3,269	133,643	177,120	(17,223)	(7,258)	289,551
Capital increase of Phonak Holding Ltd.						
from conditional capital	1	554				555
Dividend paid by Phonak Holding Ltd.			(7,811)			(7,811)
Sale of treasury shares		154			3,297	3,451
Consolidated net income			25,788			25,788
Currency translation differences				(3,680)		(3,680)
Balance September 30, 2003	**3,270**	**134,351**	**195,097**	**(20,903)**	**(3,961)**	**307,854**
Balance April 1, 2004	3,273	135,164	238,190	(23,577)	(3,960)	349,090
Capital increase of Phonak Holding Ltd.						
from conditional capital	5	3,066				3,071
Dividend paid by Phonak Holding Ltd.			(13,074)			(13,074)
Sale of treasury shares					3,960	3,960
Consolidated net income			41,189			41,189
Currency translation differences				3,857		3,857
Balance September 30, 2004	**3,278**	**138,230**	**266,305**	**(19,720)**	**0**	**388,093**

Notes to the Condensed Consolidated Financial Statements per September 30, 2004

1. Basis of preparation of the condensed consolidated financial statements

These unaudited financial statements are the interim condensed consolidated financial statements of Phonak Holding Ltd. and its subsidiaries for the six-month period ended September 30, 2004. These financial statements are prepared in accordance with the International Financial Reporting Standards (IFRS) on Interim Financial Reporting, IAS 34 and should be read in conjunction with the consolidated financial statements for the year ended March 31, 2004.

IFRS 3 “Business Combinations” became effective as of April 1, 2004. The adoption of IFRS 3, IAS 36 (revised 2004) and IAS 38 (revised 2004) resulted in a change in the accounting policy for goodwill. Until March 31, 2004, goodwill was:
– Amortised on a straight line basis over its expected economic useful life, not exceeding a maximum of 20 years; and
– Assessed for an indication of impairment at each balance sheet date.

In accordance with the provisions of IFRS 3:
– The Group ceased amortisation of goodwill from April 1, 2004;
– Accumulated amortisation at March 31, 2004 has been eliminated with a corresponding decrease in the cost of goodwill;
– Goodwill is tested for impairment on an annual basis in the first half year, when there are indications of impairment and, in the case of newly acquired goodwill, before the end of the financial year in which the goodwill was acquired.

The impact on the income statement for the period ended September 30, 2004 is an increase of the consolidated net income of CHF 4.2 million.

There were no other revised or new standards that became effective from April 1, 2004 that had a significant effect on the Group’s financial statements. The Group is currently assessing the potential impacts of newly published and revised Standards such as IFRS 2 “Share-based Payment”, IFRS 5 “Non-current Assets Held for Sale and Discontinued Operations” and the revised version of IAS 39 “Financial Instruments”. The accounting policies used are consistent with those used in the annual financial statements. The presentation of the interim financial statements is consistent with the annual financial statements.

The preparation of these interim consolidated financial statements requires management to make assumptions and estimates that affect the reported amounts of revenues, expenses, assets and liabilities at the date of these interim financial statements. If in the future such assumptions and estimates deviate from the actual circumstances, the original assumptions and estimates will be modified as appropriate in the year in which the circumstances change. Income tax expense is recognized based upon the best estimate of the average annual income tax rate expected for the full year.

The Phonak Group (the "Group") is involved in the development, manufacture and distribution of hearing systems and related products for the hearing impaired. The Group operates worldwide and distributes its products through its own distribution network in the major industrial countries and through independent representatives in over 60 other countries. The Group operates in industries where material seasonal or cyclical variations in total sales are not experienced during the financial year. The ultimate parent company is Phonak Holding Ltd., a limited liability company incorporated in Switzerland. Phonak Holding Ltd. registered office is located at Laubisrütistrasse 28, CH-8712 Stäfa, Switzerland.

2. Changes in group structure

In April 2004, Phonak acquired a 100% interest in Unitron (Sichuan) Hearing Technology Co., Ltd. (Chengdu, People's Republic of China). The acquisition was accounted for using the purchase method of accounting. The company was later renamed Phonak (Sichuan) Co., Ltd., which then acquired the assets of KAM Hearing Technology (Guangzhou) Co. Ltd. (Guangzhou, People's Republic of China). The purchase price, assets acquired, turnover and net operating result related to these acquisitions are not material to the consolidated figures at September 30, 2004.

3. Segment information

The Group is active in only one segment: the development, production, distribution and service of hearing instruments and related products. The primary segment information is presented according to geographical regions, which also correspond to the organisational structure. Transactions between segments are generally conducted at market rates.

	Europe	North America	Australasia	Eliminations/others	Total
Six months ended September 30, 2003 (1,000 CHF)					
Sales					
Third parties	137,110	152,597	13,181	(1,969)	300,919
Sales within the same segment	18,289	7,640	19	(25,948)	0
Intersegment sales	120,358	1,723	2,665	(124,746)	0
Total sales	**275,757**	**161,960**	**15,865**	**(152,663)**	**300,919**
Operating profit / (loss) (EBIT)	**56,431**	**13,227**	**(494)**	**(34,243)**	**34,921**
Financial expense, net					(469)
Income before taxes and minority interests					**34,452**
Taxes					(8,344)
Minority interest in associates					(320)
Consolidated net profit					**25,788**
Total assets	**1,043,426**	**408,274**	**20,180**	**(841,459)**	**630,421**
Total liabilities	**657,567**	**235,682**	**11,327**	**(583,095)**	**321,481**
Other information:					
Investments in tangible and intangible assets	6,104	1,392	1,075	(49)	8,522
Depreciation on tangible assets	7,388	2,614	167	0	10,169
Depreciation on intangible assets					
and write-offs of other investments	543	2,185	0	1,895	4,623

	Europe	North America	Australasia	Eliminations/others	Total
Six months ended September 30, 2004 (1,000 CHF)					
Sales					
Third parties	156,283	153,310	18,501	(3,062)	325,032
Sales within the same segment	23,100	11,446	11	(34,557)	0
Intersegment sales	115,826	11,164	10,823	(137,813)	0
Total sales	**295,209**	**175,920**	**29,335**	**(175,432)**	**325,032**
Operating profit / (loss) (EBIT)	**64,288**	**17,527**	**(1,807)**	**(24'029)**	**55,979**
Financial expense, net					(771)
Share of loss in associated company	(373)	0	0	0	(373)
Income before taxes and minority interests					**54,835**
Taxes					(13,247)
Minority interest in associates					(399)
Consolidated net profit					**41,189**
Total assets	**1,123,499**	**419,169**	**39,936**	**(883,729)**	**698,875**
Total liabilities	**652,617**	**224,050**	**33,588**	**(600,975)**	**309,280**
Other information:					
Investments in tangible and intangible assets	7,906	1,861	950	0	10,717
Depreciation on tangible assets	8,765	2,421	430	0	11,616
Depreciation on intangible assets					
and write-offs of other investments	0	0	0	0	0

4. Earnings per share

The basic earnings per share are calculated by dividing the consolidated net income by the weighted average number of shares outstanding (net of treasury shares) during the period. For the current business year, the weighted average number of shares outstanding amounted to 65,414,067 shares (previous year 65,127,230 shares). The diluted earnings per share consider the dilutive effect which could arise upon the possible exercise of all outstanding options. The weighted average number of shares used to determine the diluted earnings per share was 66,181,626 shares (previous year 65,323,118 shares).

5. Contingencies

There have been no material changes in contingent liabilities since March 31, 2004.

6. Share capital, capital reserves and treasury shares

A dividend in respect of 2003/04 of 0.20 per share, amounting to a total of CHF 13,074,000 (prior year 0.12 per share, amounting to a total of CHF 7,811,000), was paid in July 2004 to all shares outstanding, excluding treasury shares.

April to September 2003 (1,000 CHF)	**Outstanding shares**	**Share capital**	**Capital reserves**	**Treasury shares**
Opening balance April 1, 2003	65,041,590	3,269	133,643	(7,258)
Purchase of treasury shares, net	188,868	0	154	3,297
Issue of new shares from conditional capital	30,000	1	554	0
Closing balance September 30, 2003	**65,260,458**	3,270	**134,351**	**(3,961)**

April to September 2004 (1,000 CHF)	**Outstanding shares**	**Share capital**	**Capital reserves**	**Treasury shares**
Opening balance April 1, 2004	65,320,488	3,273	135,164	(3,960)
Sale of treasury shares, net	141,712	0	0	3,960
Issue of new shares from conditional capital	92,500	5	3,066	0
Closing balance September 30, 2004	**65,554,700**	**3,278**	**138,230**	**0**

Investor Relations Calendar

June 7, 2005
Annual Report per March 31, 2005
Presentation to Media and Financial Analysts

July 7, 2005
General Meeting of Phonak Holding Ltd.

November 2005
Semi-Annual Report per September 30, 2005

The Art and Science of Better Hearing

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This report is also available in German.
The English version is the governing text.

PHONAK
hearing systems