

# Question and Answer

## Operator

[Operator Instructions] Your first question comes from the line of Tristan Joll of UBS.

## Tristan Joll

*UBS Investment Bank, Research Division*

Just a few things. So on the constant currency revenue growth, Mike, I noticed you used the phrase, "core constant currency growth of mid-teens." Back at the AGM, you said you expect that this half to be 14%, but we've booked 12%. Is this because the other category is weaker or has there been some sort of change in the outlook that you had a few months ago around the core product or not?

## Michael Grenfell Daniell

*Non-Executive Director*

In the other category, we have infant warmers, which as you know, have been declining and don't see as being a long term or part of the business. We had a pretty steep decline in the first half, and that just took the edge off that growth. And so we were pleased for our core products, between respiratory and OSA, to be at the growth we expected, but the warmers are what brought us down to 12%.

## Tristan Joll

*UBS Investment Bank, Research Division*

Right. So that is the difference between sort of late August and now?

## Michael Grenfell Daniell

*Non-Executive Director*

Yes.

## Tristan Joll

*UBS Investment Bank, Research Division*

Okay, cool. And then just on the margin expansion, clearly that's a large number. I just wondered if you could give us a bit of a breakdown in terms of perhaps Mexico versus mix versus productivity in terms of what things are contributing to the 457. And when we look forward and we think about the 100 to 200 going forward, which of those 3 things is probably providing the growth?

## Michael Grenfell Daniell

*Non-Executive Director*

Sure. Well, in order of magnitude, it's coming from product mix, followed by Mexico manufacturing growth, followed by other efficiencies, our lean manufacturing, logistics and the like. And on improving [ph], you could think about 1/3 from each of those, but it's a little bit heavier weighted towards product mix. And then looking into the future, we are expecting around 1/2 of the gains in the future to come from Mexico manufacturing, and the other 1/2 to come from a combination of product mix and other efficiencies.

## Tristan Joll

*UBS Investment Bank, Research Division*

Okay, that's great. And then just one more, if I can. I just -- so noted your comments around guidance. I just wondered if you could tell us what constant currency operating profit assumption you've got in there. I think previously I felt it was going to be about 40% for the full year. I'm just trying to get a sense of how much this apparent earnings upgrade is actually an underlying increase?

## Michael Grenfell Daniell

*Non-Executive Director*

Well, we are saying 40% for the full year is all we're saying.

**Operator**

[Operator Instructions] Your next question comes from the line of Stephen Ridgewell of Craigs Investment.

**Stephen Ridgewell**

*Craigs Investment Partners Limited, Research Division*

The first question for me, just in terms of operating leverage, can you just comment on -- you took the operating leverage in the half, are you still planning to take some more leverage in FY '16? And if so, is that likely to be coming out of the OSA business, respiratory, and perhaps by geography? Are there any particular markets you think you can take leverage on?

**Michael Grenfell Daniell**

*Non-Executive Director*

As we move into FY '16, we are expecting R&D to grow at fairly close to underlying revenue growth and constant currency. We do expect to take a couple of percentage points on SG&A, some of that in G&A and a little in S, in sales. We're delivering more and more products and a broader range and better products to our sales teams, and so they're generating more sales per head. So we can get some leverage from that. And that's reasonably uniform around the world.

**Stephen Ridgewell**

*Craigs Investment Partners Limited, Research Division*

And also uniform between OSA and respiratory?

**Michael Grenfell Daniell**

*Non-Executive Director*

Yes, yes.

**Stephen Ridgewell**

*Craigs Investment Partners Limited, Research Division*

All right. And can you just touch on the 26% growth you're seeing in the new products in RAC? And was it mainly being driven by higher flow, oxygen and COPD? Is that related to strong growth in the half?

**Michael Grenfell Daniell**

*Non-Executive Director*

The bigger component is our Optiflow therapy, which applies right through adult care and right through to neonates, and that was the biggest contributor. We also saw good growth in adoption of humidification into noninvasive ventilation. And we saw very good growth off a much smaller base in our surgical application as well.

**Stephen Ridgewell**

*Craigs Investment Partners Limited, Research Division*

And just the flow generator growth number that you reported, are you starting to see a little bit of AIRVO coming through on that number?

**Michael Grenfell Daniell**

*Non-Executive Director*

Yes, AIRVO. AIRVO is a flow generator as well, and that's a contributor to that.

**Stephen Ridgewell**

*Craigs Investment Partners Limited, Research Division*

Great. And just last one for me. The guidance that you've just given for mid-teens constant currency growth for both divisions, are you including OSA for the full year? And is this essentially, you're certainly

not seeing any particular market share shift in OSA, is that a fair observation, aside from positive, I should say? You're not seeing ResMed or Respirationics take share obviously based on that guide?

**Michael Grenfell Daniell**

*Non-Executive Director*

It's hard to know given there's fairly incomplete reporting today of any other company's actual OSA revenue. We believe we are growing at about double the market growth rate.

**Stephen Ridgewell**

*Craigs Investment Partners Limited, Research Division*

Right. And so you don't seem to be seeing any impact or material impact to date from ResMed's product cycle?

**Michael Grenfell Daniell**

*Non-Executive Director*

Well, we have just provided guidance, and we expect growth to continue pretty strongly in the second half.

**Operator**

Your next question comes from the line of Victor Windeyer of Citi.

**Victor Windeyer**

*Citigroup Inc, Research Division*

I just wanted -- I missed the guidance on tax rate going forward and can you just give a bit of more detail on why the tax rate will be lower in this period?

**Antony G. Barclay**

Sure. It's Tony here. The tax rate is a little bit lower in the first half as we've hit some foreign currency translation that goes through our P&L that doesn't attract a tax expense. And the guidance was other than currencies moving around, we'd expect that our effective tax rate to be about 29%.

**Operator**

Your next question comes from the line of Nachi Moghe of Morningstar Research.

**Nachiket Moghe**

*Morningstar Inc., Research Division*

A couple of questions. One is on AIRVO. I was just wondering how far are you from getting a reimbursement in the home setting for AIRVO? And the other one was in terms of OSA. Are you likely to launch a couple of new products in the back half of this year, second half of this year? Just wondering because the last, I think, new products that you launched in OSA was back, I think, in November, if my memory serves me right. So can you just provide me some color on that?

**Michael Grenfell Daniell**

*Non-Executive Director*

AIRVO is being paid for in a number of countries, but we don't yet have any specific reimbursement codes. And the way that usually works is, you need to build up a reasonable base of patients before you can get a code. So we're engaged in there. Hard to predict in terms of timing on reimbursement codes, but we're hopeful that we will get codes in a number of countries over the coming year or 2. With respect to new products, we're not in a position to announce the timing of any new products at present, although we don't expect anything meaningful in the next -- in the second half of this year.

**Operator**

Your next question comes from the line of Sarndra Ulrich of First NZ Capital.

**Sarndra Ulrich**

*Jarden Limited, Research Division*

Just an admin question, just on the currency, just the usual question. Just -- if I just -- just reconciling the constant currency PBT at \$46 million and the profit before tax at \$67 million, and so that \$21 million currency related difference. In terms of how I should just assuming the currency, just all things being equal, in terms of the FY '15 outlook, how much -- and I know you're going to say there's lots of variables around that, but in terms of how much of -- how much should I expect that to be for the full year?

**Antony G. Barclay**

Sarndra, in terms of the forecast -- built into the forecast for hedging gains, that's around \$29 million for the full year.

**Sarndra Ulrich**

*Jarden Limited, Research Division*

So \$29 million. And that includes -- well, it's just -- so that's all 3 of those things. That's okay. So that's \$29 million for the full year. Okay, so there's probably another \$8 million.

**Antony G. Barclay**

And on top of that, a little bit of balance sheet translation, positive if we stay where we are, so about \$3 million.

**Sarndra Ulrich**

*Jarden Limited, Research Division*

Okay. So maybe \$11 million assuming all that, including balance sheet translation. Cool.

**Antony G. Barclay**

And we're seeing whole with the balance sheet, translation has pretty much already happened in the first half. Today's exchange rates were about where we ended the half.

**Sarndra Ulrich**

*Jarden Limited, Research Division*

Yes. And just in terms of -- just so I make sure I'm not missing anything. From a -- in terms of the reimbursement, now that we have cycled through CB 2 and 3 [ph], just -- and there's always iterations around reimbursement. But just to make sure I'm not missing anything, the bundling proposition that was put forth for FY '16, and I know it was just a proposition, have you heard any news as to whether that becomes definitive or any progress being made there? Have you talked to the DME working it and the states or has it just gone quiet?

**Paul N. Shearer**

*Senior Vice President of Sales & Marketing*

Sarndra, Paul here. My understanding is that in terms of bundling trial, that's being pushed out to 2017. And that I think that trial will last 2 or 3 years.

**Operator**

There are no further questions at this time. Please continue.

**Michael Grenfell Daniell**

*Non-Executive Director*

Perhaps, Leah, you could give one more opportunity.

**Operator**

[Operator Instructions] Your next question comes from the line of Ian Abbott of Goldman Sachs.

**Ian Abbott**

*Goldman Sachs JBWere Pty Ltd, Research Division*

I was just wondering if you could perhaps give a sense of what you think new patient growth is in the U.S. at the moment in OSA? Or if you think the market is actually growing in terms of the flow of new patients this year or new patients last year?

**Paul N. Shearer**

*Senior Vice President of Sales & Marketing*

Paul here, Ian. That's a very difficult question to answer. Of course, those information not available, but we think it's growing. We think it's probably modest growth. Probably we're saying that -- we're thinking maybe around that 6%, 6% to 8% mark possibly.

**Ian Abbott**

*Goldman Sachs JBWere Pty Ltd, Research Division*

All right. And then secondly, just in your conversations and assessment of DMEs post all of the price concessions that the suppliers have given over the last 18 months, what is your sense of their financial health at present? Do you think that they're now in a position where they're on a sustainable footing or are they still in sort of semi-crisis mode such that they will need further concessions down the track or sort of further consolidation to put them into a sustainable position.

**Michael Grenfell Daniell**

*Non-Executive Director*

So I think most of the home care providers are at pretty stable mode actually. I mean, when you actually think about competitive biddings being around for quite a while now. They have been operating in this environment for quite a lengthy period of time. We're rarely seeing, we've haven't actually really seen a lot of our customers even go out of business. So I think they have adapted to the environment, the changing landscape and, in fact, that's the reason they're stable.

**Ian Abbott**

*Goldman Sachs JBWere Pty Ltd, Research Division*

And so I suppose the follow-on question then is, would you say that pricing then is -- do you get a sense that pricing activity, I mean, I know it's always competitive, and they're always deals being done. But is your sense that that sort of step change you saw 6 and 12 months ago, we're sort of through that now?

**Michael Grenfell Daniell**

*Non-Executive Director*

We're clearly out of it. And as you can see from what we just said in our announcement today that what's happened to us as a company, we're well in that 2% to 5% band. I think it's a pretty stable market now. It's competitive as always, but I think that we're definitely through that period of erosion that occurred over the last couple of years.

**Ian Abbott**

*Goldman Sachs JBWere Pty Ltd, Research Division*

Okay. And one final question on again on OSA. Can you comment just on your growth in rest of world outside Europe and the U.S.? Talk about sort of which countries or which areas, apologies if I missed it in the announcement, but in terms of some of the markets outside sort of those traditional markets which are doing well.

**Michael Grenfell Daniell**

*Non-Executive Director*

So is that in relation to OSA, you were asking a question?

**Ian Abbott**

Goldman Sachs JBWere Pty Ltd, Research Division

Yes, yes.

**Michael Grenfell Daniell**

*Non-Executive Director*

We're seeing pretty decent growth outside the States around the rest of the world. I won't go into specific markets, but we've been seeing growth in most of the markets we've been doing business. And it's at a relatively similar rate.

**Operator**

The next question comes from the line of Sarndra Ulrich of First NZ Capital.

**Sarndra Ulrich**

*Jarden Limited, Research Division*

Mike, sorry I just missed the last comment. Sorry, I was asking a question, they put me on music. The question about the new product I missed, can you please repeat what you said about what are the new products in the second half? I missed what you said there.

**Michael Grenfell Daniell**

*Non-Executive Director*

I didn't really say anything there, Sarndra. We're not in a position to be talking about timing of that broad range of new products we've got, but I did say that we had nothing significant planned in the second half.

**Operator**

The next question comes from the line of Nachi Moghe of Morningstar.

**Nachiket Moghe**

*Morningstar Inc., Research Division*

Just Mike, I think in the -- in your remarks, you mentioned about surgery. I'm just wondering, what sort of growth are you seeing in that application at the moment and is that mainly coming from the U.S. or international?

**Michael Grenfell Daniell**

*Non-Executive Director*

We're seeing strong growth, much faster than overall growth in the business, off a pretty small base though to be fair. And we're making very, very good progress in terms of clinical evidence to show the benefits of providing humidified CO2 during surgery. We're currently selling in Australasia and in Europe. We haven't entered the U.S. market yet. So all of that growth is coming from those 2 regions.

**Nachiket Moghe**

*Morningstar Inc., Research Division*

Right, right. And when do you expect to sell this product in the U.S.? Probably in the U.S., when do you expect to be in the U.S.?

**Michael Grenfell Daniell**

*Non-Executive Director*

Probably more than a year away yet. We are learning as we go here. This is a new market for us in the surgical environment, and we're happy with the progress we're making where we are. But we'd like to make more progress here before we enter the U.S. market.

**Nachiket Moghe**

*Morningstar Inc., Research Division*

Right. And in terms of competition, are there any significant competitors in this space?

**Michael Grenfell Daniell**

*Non-Executive Director*

No. We are pioneering in this space, but we do see a very good opportunity there.

**Operator**

There are no further questions at this time. Please continue.

**Michael Grenfell Daniell**

*Non-Executive Director*

Okay. Well thank you, Leah, and thank you, everyone, for joining us on the call today. Obviously, our teams here in New Zealand and around the world are very committed to delivering innovative devices which are improving care and outcomes for a growing number of patients. The team is more than 3,000 strong now, and we would like to acknowledge and thank them for their outstanding efforts and the results that we are achieving. Thank you, all, for joining us today. And we'll talk to you next time.

**Operator**

Ladies and gentlemen, that does conclude our conference for today. Thank you, all, for participating. You may all disconnect.