At a glance

Smith & Nephew is a leading portfolio medical technology company

<table>
<thead>
<tr>
<th>OUR PURPOSE</th>
<th>HIGHLIGHTS</th>
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<tbody>
<tr>
<td><strong>Life Unlimited</strong></td>
<td><strong>REVENUE</strong></td>
</tr>
<tr>
<td>Smith &amp; Nephew exists to restore people’s bodies, and their self-belief.</td>
<td><strong>$4,904m</strong></td>
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**OUR CULTURE PILLARS**

<table>
<thead>
<tr>
<th>Care</th>
<th><strong>REVENUE BY GEOGRAPHY</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td>A culture of empathy and understanding for each other, our customers and patients</td>
<td>United States $2,354m</td>
</tr>
<tr>
<td><strong>Collaboration</strong></td>
<td>Other Established Markets $1,693m</td>
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<tr>
<td>A culture of teamwork based on mutual trust and respect</td>
<td>Emerging Markets $857m</td>
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<tr>
<td><strong>Courage</strong></td>
<td></td>
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<tr>
<td>A culture of continuous learning, innovation and accountability</td>
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**OUR STRATEGIC IMPERATIVES**

<table>
<thead>
<tr>
<th>Five new strategic imperatives form our value creation plan for the medium term.</th>
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<tbody>
<tr>
<td>1. Achieve the full potential of our portfolio</td>
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<td>2. Transform the business through enabling technologies</td>
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<td>3. Expand in high-growth segments</td>
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<tr>
<td>4. Strengthen talent and capabilities</td>
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<tr>
<td>5. Become the best owner</td>
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**MANUFACTURING & QUALITY**

Smith & Nephew takes great pride in its expertise in manufacturing products to the highest quality and ensuring they reach our customers in a timely manner.

<table>
<thead>
<tr>
<th>EMPLOYEES</th>
<th><strong>YEARS</strong></th>
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<tbody>
<tr>
<td><strong>16,000+</strong></td>
<td><strong>160+</strong></td>
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</table>

<table>
<thead>
<tr>
<th>COUNTRIES SUPPORTING HEALTHCARE PROFESSIONALS</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>100+</strong></td>
<td></td>
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</table>
OUR GLOBAL FRANCHISE AREAS

ORTHOPAEDICS
Orthopaedics includes an innovative range of Hip and Knee Implants used to replace diseased, damaged or worn joints and Trauma products used to stabilise severe fractures and correct bone deformities.

SPORTS MEDICINE & ENT
Our Sports Medicine and Ear, Nose and Throat (ENT) businesses offer advanced products and instruments used to repair or remove soft tissue. They operate in growing markets where unmet clinical needs provide opportunities for procedural and technological innovation.

ADVANCED WOUND MANAGEMENT
Our Advanced Wound Management portfolio provides a comprehensive set of products to meet broad and complex clinical needs, to help healthcare professionals get CLOSER TO ZERO human and economic consequences of wounds.

OUR NEW COMMERCIAL STRUCTURE
In 2018, we initiated substantial changes to our commercial organisation to move to a franchise-led model from January 2019. Under this, a president leads each of our three specialised global marketing franchises – Orthopaedics, Sports Medicine & ENT and Advanced Wound Management. Aligned with and supporting the franchises are presidents and regional commercial organisations for Europe, Middle East, and Africa (EMEA), and Asia Pacific (APAC). The franchise presidents also have commercial responsibility for the US.

INNOVATION
Smith & Nephew delivers innovation that aims to improve quality of life. New products and business models enable healthcare professionals to offer patients improved outcomes. We develop technology through our global R&D programme, and additionally acquire exciting products where we can add value through technical or commercial acumen.

10% MORE INVESTED IN R&D IN 2018

$246m
DEAR SHAREHOLDER

2018 was a busy year for Smith & Nephew. Performance improved across the year, whilst the Company underwent a period of significant transformation, in leadership, structure, culture and strategy.

CHIEF EXECUTIVE OFFICER

In 2017, Olivier Bohuon told us he intended to retire after more than seven years as Chief Executive Officer. Under his leadership, Smith & Nephew experienced important and necessary change and he significantly strengthened the foundations of our Company. I would like to take this opportunity to thank him for his service and wish him a long and healthy retirement.

In May 2018, Namal Nawana joined Smith & Nephew as Chief Executive Officer and was appointed to the Board as an Executive Director.

Namal is a global industry insider, an innovator, and proven leader. Most recently, he was Chief Executive Officer, President and a member of the Board of Directors of medical diagnostics company Alere, Inc. Here he led the successful turnaround of this global business before its acquisition by Abbott Laboratories in 2017.

Before joining Alere, Namal spent more than 15 years at Johnson & Johnson, in roles of increasing responsibility in Europe, Asia and North America, culminating in Worldwide President of DePuy Synthes Spine. We were delighted when he agreed to join Smith & Nephew.

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Financial highlights

REVENUE

$4,904m

Reported +3%

Underlying +2%

Group revenue was up 3% on a reported basis (including 1% from foreign exchange tailwind) and 2% on an underlying basis.

DIVIDEND PER SHARE

36.0¢ +3%

The 3% year-on-year increase reflects the growth in adjusted earnings and is in-line with our progressive policy.

EARNINGS PER SHARE (EPS)

76.0¢ -13%

The decrease reflects the impact of the restructuring charges relating to the APEX programme.

ADJUSTED EARNINGS PER SHARE (EPSA)

100.9¢ +7%

The increase reflects improved trading performance and lower tax rate on trading.

RETURN ON INVESTED CAPITAL (ROIC)

12.5% -180bps

The decrease reflects primarily the fall in operating profit.

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1 These non-IFRS financial measures are explained and reconciled to the most directly comparable financial measures prepared in accordance with IFRS on pages 194–198.
Chair’s statement

A period of significant transformation; in leadership, structure, culture and strategy

LEADERSHIP & CULTURE
Since May, Namal has worked closely with the Board. We have reviewed and endorsed his actions to restructure the Company. He has rapidly built a highly experienced new leadership team, bringing in strong external leaders as well as promoting from within Smith & Nephew. Members of this team meet regularly with the Board, and we have seen for ourselves the clear focus and strong collaboration across this team.

The Board has long held culture as an important indicator of the underlying health of the Company. We have welcomed the importance Namal has placed on this, and his purpose and the behaviours all employees must display to deliver the strategy. This was not an academic exercise, or conducted by just the senior management team, but rather a case study in how to engage employees, with 6,000 employees contributing to the process. The Board believes that the new structure, culture and strategy are both authentic and inspiring.

STRATEGY
In December, the Board approved the new strategic imperatives that will drive value creation in the medium term. This was a culmination of a collaborative process between the Board and the Chief Executive Officer and senior leadership team over a number of months. During this process we tested their insight of, and vision for, the medical technology industry and found their analysis of the opportunities the Company faces was detailed and compelling.

The five strategic imperatives are similarly robust. The Board welcomes their wide-ranging scope – to accelerate growth, both organically and through acquisitions, strengthen people and capabilities, and improve the operations of our business globally.

2018 PERFORMANCE
The Board closely monitors the performance of the business through regular updates from the Chief Executive Officer and Chief Financial Officer and other members of the senior leadership team.

2018 performance was solid, with an improved dynamic in the second half. The Board noted how well the new team delivered this acceleration whilst also undertaking important work to restructure the Group. Whilst there is still much work to be done, the new Group structure is now in place. The Board endorses the guidance for further progress in 2019.

The Board is pleased that shareholders will benefit from strong growth in adjusted earnings per share, which is reflected in the 3% increase in the full year dividend to 36.0 cents per share. The performance of our shares is also noteworthy, increasing 13% from when Namal joined up to the end of 2018, strongly outperforming the FTSE 100.

BOARD CHANGES
During 2018, we welcomed Roland Diggelmann as a Non-Executive Director.

Roland was, until recently, Chief Executive Officer of Roche Diagnostics and a member of the Corporate Executive Committee of F. Hoffmann-La Roche Ltd. He brings direct experience in orthopaedics from previous senior roles at Zimmer.

Ian Barlow will step down from the Board at the Annual General Meeting in April 2019, having completed a nine-year term. Ian has served Smith & Nephew with great distinction as our Senior Independent Director, and previously as Chair of the Audit Committee. I have been grateful for his counsel and thank him for his significant contribution over the years.

Michael Friedman, Chair of our Compliance & Culture Committee, will also be retiring at that time after six years’ service, and I thank him for his leadership in this crucial area.

Robin Freestone will replace Ian as Senior Independent Director and Marc Owen will replace Michael as Chair of the extended Compliance & Culture Committee.

Smith & Nephew values diversity, and I am pleased that this is reflected in our Board, which, following these changes will be 30% female and include six nationalities. We continue to look for opportunities to widen our outlook and expertise with an expanded mandate.

The phrase ‘step change’ is used too often, but today I believe that Smith & Nephew stands at the start of such a transformation. Whilst there is still much work to be done, the Board is excited by the prospects and looks forward to supporting the new management team as they realise Smith & Nephew’s full potential.

Yours sincerely,

Roberto Quarta
Chair

The phrase ‘step change’ is used too often, but today I believe that Smith & Nephew stands at the start of such a transformation.

Roberto Quarta
Chair

Smith & Nephew Annual Report 2018
Chief Executive Officer’s review

At Smith & Nephew, we aspire to be amongst the highest-performing portfolio medical technology companies

DEAR SHAREHOLDER

Everyone has health issues at some stage in their life. At Smith & Nephew, we have the opportunity to help patients get back to their lives as quickly as possible, and as well as possible. Whether it be in Orthopaedics, Sports Medicine or Wound Management we recognise this opportunity and it inspires and motivates our work each day around the world.

CREATING A PURPOSE-DRIVEN CULTURE

I believe that a successful and sustainable business has a foundation that is built on a purpose-driven culture. When I joined, we asked our employees which elements of our culture they liked and that we should retain, as well as what we needed to improve at Smith & Nephew. 6,000 employees responded.

It was clear that our colleagues cared deeply about the work that we do. It was also clear that they recognised that we could do better. The opportunity was to find an authentic and inspiring purpose that combines this caring spirit with a greater focus on working more effectively and instilling a strong accountability to deliver consistently on our commitments.

Life Unlimited captures the essence of Smith & Nephew and our purpose to address meaningfully the health issues that hinder people from living their lives to their fullest.

To support this brand purpose we have developed three culture pillars: Care, Collaboration and Courage – which we launched with employees at the end of 2018. Grounded in the service of patients and practitioners, these simple tenets guide us in our work together and couple the idea of continuous learning and improvement with the aspiration to lead in all our endeavours.

OUR BUSINESS AND STRATEGIC IMPERATIVES

Smith & Nephew is a portfolio medical technology company with a broad and deep range of high quality products. We have examples of market-leading technology in almost every area of our business. We also operate in large and attractive global markets, with solid long-term growth prospects supported by favourable demographics and lifestyle trends.

At the end of 2018, we launched five new strategic imperatives that recognise the specific business and markets we operate in, and form the basis of our value creation plan for the medium-term.

1. Achieve the full potential of our portfolio
2. Transform the business through enabling technologies
3. Expand in high-growth segments
4. Strengthen talent and capabilities
5. Become the best owner

These highlight the key multi-year initiatives in which the Company is now engaged. They also detail the specific plans and metrics for the upcoming calendar year from which all employees build their own individual annual objectives.

INCREASING CUSTOMER CENTRICITY

One of the most significant changes we are making is implementing a new commercial model. In line with industry best practice for global medical technology businesses, we are moving from a regional selling model to a global franchise structure. We have put dedicated presidents of Orthopaedics, Sports Medicine & ENT, and Advanced Wound Management in place.

Each president has global upstream marketing responsibility, as well as full commercial responsibility for the franchise in the US. Outside the US, we will have two regions, Europe, Middle East and Africa, and Asia Pacific. Both regions are now represented on the Smith & Nephew Executive Committee ensuring continued focus on commercial execution. As specialists, the presidents bring great insight into our customers’ current and future needs, wherever they are in the world and will be able to direct the full resources of their franchises to meet these.

I am delighted with the quality of leaders we have attracted. The focus is now on unlocking the potential of Smith & Nephew, with five members of my executive team directly responsible for driving growth in their franchises and regions.
Smith & Nephew completed 2018 with a net debt\(^1\) to adjusted EBITDA ratio\(^2\) of 0.8x and, with strong cash flows and cash conversion, we will look to appropriately deploy capital to M&A initiatives more significantly than in recent years as part of our business model for success.

Technology acquisitions such as Rotation Medical have proven to be a great success. From its REGENETEN\(^\text{®}\) Bioinductive Implant for rotator cuff repair, we have driven performance well-ahead of our deal model, with more than 130% growth in 2018. We believe there is still much more to come from this product as we add manufacturing capacity and launch in new international markets in 2019.

In December, we announced the acquisition of Ceterix Orthopaedics, the developer of the NovoStitch\(^\text{®}\) Pro Meniscal Repair System. This product is highly complementary to our portfolio and will significantly expand our opportunity in the underserved meniscal repair segment.

I expect us to continue to enhance our position in high-growth, high-innovation markets over time and capitalise on our platform as a global medical device portfolio company.

I am delighted with the quality of talent we have attracted. The focus is now on unlocking the potential of Smith & Nephew, with five members of my executive team directly responsible for driving organic growth in their franchises and regions.

Namal Nawana
Chief Executive Officer

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1 Net debt is reconciled in Note 15 to the Group accounts.
2 These non-IFRS financial measures are explained and reconciled to the most directly comparable financial measure prepared in accordance with IFRS on pages 194–198.
Our culture pillars

A successful business needs to have a purpose-driven culture

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**Life Unlimited**

Life Unlimited captures the essence of Smith & Nephew and our purpose to address meaningfully the health issues that hinder people from living their lives to their fullest.

Namal Nawana
Chief Executive Officer

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<table>
<thead>
<tr>
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<th>COLLABORATION</th>
<th>COURAGE</th>
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</thead>
<tbody>
<tr>
<td>A culture of empathy and understanding for each other, our customers and patients</td>
<td>A culture of teamwork, based on mutual trust and respect</td>
<td>A culture of continuous learning, innovation and accountability</td>
</tr>
<tr>
<td>– We step into our customers’ shoes, anticipate their needs and deliver the highest levels of innovation and service</td>
<td>– We are stronger, and achieve more, as a team. By joining forces we are both unstoppable and efficient</td>
<td>– By staying curious, thinking big and having the humility to challenge our conventional ways of thinking, we push the boundaries of our industry</td>
</tr>
<tr>
<td>– We strive to have the best understanding of the patients whom we ultimately serve, and we develop our products with them in mind</td>
<td>– Through transparent and respectful communication, we are motivated by a shared purpose and understand the impact of our individual contributions on our collective goals</td>
<td>– Fostering an entrepreneurial, can-do attitude we look for solutions and achieve them through talent and force of will</td>
</tr>
<tr>
<td>– Our passion for what we do drives us to continuously improve and expand the positive impact that we have on the world</td>
<td>– By encouraging different perspectives and leveraging our global experiences, we achieve the best outcomes</td>
<td>– With a growth mindset, we have the capability and confidence to win, and we do so with integrity and the highest ethical standards</td>
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Our strategic imperatives

Five new strategic imperatives form our value creation plan for the medium term

<table>
<thead>
<tr>
<th>GROW</th>
<th>TOGETHER</th>
<th>EFFECTIVELY</th>
</tr>
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<tbody>
<tr>
<td><strong>1</strong></td>
<td><strong>2</strong></td>
<td><strong>3</strong></td>
</tr>
<tr>
<td>Achieve the full potential of our portfolio</td>
<td>Transform the business through enabling technologies</td>
<td>Expand in high-growth segments</td>
</tr>
<tr>
<td>Improving execution to accelerate organic performance with a focus on (i) platform-specific plans, (ii) Ambulatory Surgery Centres and (iii) Emerging Markets, especially China and Latin America.</td>
<td>By acquiring and developing leading enabling technologies to transform procedures, including robotics, imaging and augmented reality.</td>
<td>By accelerating portfolio growth, strengthening or establishing leadership positions, and driving meaningful synergies.</td>
</tr>
</tbody>
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| | | |
| **4** | **5** | |
| Strengthen talent and capabilities | Become the best owner | |
| By developing a winning culture to improve retention and attract talent. | To drive meaningful margin expansion through operational transformation and organisation simplification. | |

MEASURING PERFORMANCE

Behind our strategic imperatives sits a detailed dashboard of key performance indicators that we use to track and evaluate our performance. These cover Commercial, Operations, R&D, People, our SG&A and cost base, as well as return on investment and cash.

Whilst many of these are commercially sensitive, and hence will not be published, they all support our objective to deliver on our financial guidance for 2019. This is detailed in the CFO review on page 37.

Other published metrics include our work to simplify the organisation and processes through our restructuring programme APEX, and our focus on turning profit into cash. These are also described in more detail in the CFO review.

2018 KPIs were set against previous strategic priorities. These measured revenue growth in our Established and Emerging Markets, operating and trading profit margin and R&D investment. These measures are reported on page 4.
Our markets

Competing in large, attractive markets

The healthcare sector is a growing market driven by long-term trends. Global healthcare spend amounted to $7.7 trillion, or 10.4% of global GDP in 2017, and is projected to increase at an annual rate of 5.4% over the five year period to 2022.*

The medical devices and supplies segment of healthcare is today worth more than $400 billion per annum. Within that, Smith & Nephew’s product segments are worth approximately $36 billion, growing at around 4% annually.

The main drivers for healthcare demand include demographic shift towards ageing populations and an increase in lifestyle-related ailments such as diabetes and obesity. The World Health Organisation (WHO), for example, states that obesity has nearly tripled since 1975 worldwide – a major risk factor for diseases such as diabetes and musculoskeletal disorders.

Faster growing emerging markets with an emerging middle class also drive demand. The Brookings Institute estimates that 65% of the global population will be middle class by 2030. Access to middle class comforts encourages sedentary lifestyles that may lead to greater incidence of diabetes, obesity and other health conditions. Wealthier patients also try to exert more choice over healthcare and have greater expectation of quality of life.

The number of people aged 60 years and older will outnumber children younger than five years by 2020, according to WHO. This change in dynamic puts healthcare providers and governments increasingly under economic pressure. Politicians seek ways to reduce overall healthcare expenditure whilst maintaining the quality of care and treatment provided.

A HIGHLY REGULATED INDUSTRY

The medical device sector is highly regulated. This is vital in determining whether products are both safe and effective.

National regulatory authorities administer and enforce a complex series of laws and regulations that govern the design, development, approval, manufacture, labelling, marketing and sale of healthcare products. They also review data supporting the safety and efficacy of such products. In many countries, there is a requirement for products to be authorised or registered prior to entering the market, and such authorisation or registration needs to be subsequently maintained. For example, the US Food and Drug Administration (FDA) continues to enforce an increase in the amounts of testing and documentation required for FDA approval of new drugs and medical devices.

In Europe, the European Union Medical Device Regulations came into force in 2017 and will apply from May 2020. This will also impose tougher requirements of market entry and post-market surveillance of medical devices. Although healthcare systems are less costly in Europe than in the US, strained government budgets and demographic challenges are driving an increased focus on value-based healthcare to demonstrate the value of innovation through evidence.

The major regulatory agencies for Smith & Nephew’s products include the US FDA, the Medicines and Healthcare products Regulatory Agency (MHRA) in the UK, the Ministry of Health, Labour and Welfare in Japan, the National Medical Products Administration (NMPA) in China, formerly the China Food and Drug Administration, and the Australian Therapeutic Goods Administration.

We are subject to regular inspections and audits by regulatory agencies and notified bodies, and in some cases remediation activities have been required and will continue to require significant financial and resource investment.

**COMPLIANCE**

Interactions between medical device companies and healthcare professionals or government officials are subject to strict control. These include laws and industry codes, including the AdvaMed Code of Ethics and the Med Tech Europe Code of Business Practice.

Legislation covering corruption and bribery, such as the UK Bribery Act and the US Foreign Corrupt Practices Act, also applies to Smith & Nephew world-wide. There is also a strong focus on compliance and cost control in emerging markets such as China. We are committed to ensuring regulatory compliance globally, at all times, and to execute business with integrity.

**GEO-POLITICAL FACTORS**

Some uncertainty continues around the UK’s exit from the European Union and its regulatory impact. The European Union is the UK’s biggest export market for medical devices. Around $2 billion worth of products are sent to European countries each year.

Smith & Nephew has taken steps to prepare for the various Brexit scenarios, including moving certain of its product certifications from BSI UK to BSI Netherlands, ensuring these remain with a Notified Body domiciled in the European Union. There is also uncertainty around US-China trade relations, which has resulted in tariffs on some medical devices being exported between the two countries.

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**EVLING MODELS OF HEALTHCARE**

The traditional approach to healthcare provision has been symptom and volume (fee-for-service) oriented which – in combination with current demographic trends – has put upward pressure on healthcare costs. In response, stakeholders are increasingly seeking to shift the focus from ‘break-fix’ to a more holistic and value-based approach focused on disease prevention and treatment results (fee-for-outcome).

Healthcare practitioners are no longer the only decision-makers, but are part of larger multi-stakeholder purchasing processes. Economic stakeholders have increasing influence on the purchase process for medical devices. New payment models, such as bundled procedure payments, risk sharing, or quality incentives/penalties, are shifting the focus from clinical utility and safety alone to clinical outcomes and health economic performance.

There are a number of emerging trends which will shape our marketplace in the medium term.

There is an emerging trend for greater use of outpatient surgery. This is leading to a shift in where total joint procedures take place. Historically these have been inpatient procedures requiring an overnight stay in a hospital. With improvements in technology, more minimally invasive techniques and better pain management, total joint procedures can take place in the outpatient setting for the right patients. For example in the US there are ambulatory surgery centers (ASCs), smaller clinical units with no overnight beds. Costs are lower when no overnight stay is required, important in the context of pressure on health budgets around the world.

Other emerging trends include digital health, with connected devices monitoring patients to prevent conditions, support rehabilitation and measure outcomes. Robotics is also becoming increasingly present in the operating room, offering surgeons greater precision and consistency.

**SEASONALITY**

Some seasonality is evident in medical devices. Orthopaedic reconstruction and sports medicine procedures tend to be higher in the winter months when accidents and sports-related injuries are highest. Elective procedures tend to slow down in the summer months due to holidays. Due to the nature of our product range, there is little seasonal impact on our Advanced Wound Management franchises. The majority of our business is in the Northern Hemisphere, including approximately 50% in the US and 25% in Europe. In the US, out-of-pocket costs for health insurance plans are tied to medical expenses in a calendar year. As a result, households who have reached their deductible (or out-of-pocket) cap may find that accessing care later in the year comes at a lower cost, which may encourage some to schedule any required treatments or procedures in the final months of any given year.

**COMPETITION**

Smith & Nephew’s franchises have several competitors which differ with respect to product focus, geographic reach and overall scale. For example, our main surgical competitors are larger in scale and tend to be more exposed to the US, whereas our key wound competitors are generally not US centric.

In Orthopaedics, as one of four leading players, we compete against US-based companies Stryker, Zimmer Biomet and Depuy Synthes (a Johnson & Johnson company). In Sports Medicine, we hold a leading position behind Arthrex (US), and also compete against Stryker and Depuy Synthes.

We are the second largest global Advanced Wound Management business. We lead the somewhat fragmented Advanced Wound Care sub-segment alongside Mölnlycke (Sweden) and Convatec (UK). In Advanced Wound Devices, we are the primary challenger to Negative Pressure Wound Therapy incumbent Acelity (US). In our Advanced Wound Bioactives franchise, our key products lead their respective categories.

**MARKET SIZE**

**ORTHOPAEDICS**

<table>
<thead>
<tr>
<th>Product</th>
<th>Market Size</th>
<th>Growth</th>
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</thead>
<tbody>
<tr>
<td>Hip &amp; Knee Implants</td>
<td>$14.5bn</td>
<td>+2%</td>
</tr>
<tr>
<td>Trauma &amp; Extremities</td>
<td>$6.0bn</td>
<td>+4%</td>
</tr>
</tbody>
</table>

**SPORTS MEDICINE**

<table>
<thead>
<tr>
<th>Product</th>
<th>Market Size</th>
<th>Growth</th>
</tr>
</thead>
<tbody>
<tr>
<td>$5.0bn</td>
<td>+5%</td>
<td></td>
</tr>
<tr>
<td>$9.0bn</td>
<td>+5%</td>
<td></td>
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**ADVANCED WOUND MANAGEMENT**

<table>
<thead>
<tr>
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<th>Market Size</th>
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<tr>
<td>$5.0bn</td>
<td>+5%</td>
<td></td>
</tr>
<tr>
<td>$9.0bn</td>
<td>+5%</td>
<td></td>
</tr>
</tbody>
</table>

1 Data used in 2018 estimates generated by Smith & Nephew is based on publicly available sources and internal analysis and represents an indication of market shares and sizes.
2 Representing repair products and arthroscopic enabling technologies, and excluding ENT.
3 A division of Johnson & Johnson.
Our business model

Value creation is driven by our new brand purpose, culture pillars and strategic imperatives

OUR RESOURCES CREATING VALUE THROUGH

Our people & culture
Attracting, developing and retaining the best employees is important. We strive to build a purpose-driven culture based on strong and authentic values.

Ethics & compliance
Committed to doing business the right way, applying strict principles to the way we work.

Sales & marketing
Supporting customers through highly specialised sales teams with in-depth technical knowledge that surgeons and nurses greatly value.

Manufacturing & quality
Operating global manufacturing efficiently, to the highest standards, to ensure quality and competitiveness.

Medical education
Supporting the safe and effective use of our products through medical education.

Research & development
Innovation is part of our culture and we are increasing the amount we invest in new products.

Sustainability
We focus on three aspects of sustainability; economic prosperity, social responsibility and environmental stewardship.

Purpose-driven culture
We believe in Life Unlimited, and have three culture pillars that guide our behaviours and build a winning team spirit: Care, Collaboration and Courage.

Strong product portfolio
We have market-leading technology across our broad range of products. We deploy our capital to drive continued innovation from our R&D programmes and invest in product and technology acquisitions, which improve outcomes and widen access to life-changing care.
Strategic imperatives
Our five new strategic imperatives reflect our ambition to maximise commercial advantage from our marketplace. They will form our value creation plan for the medium term.

Customer centricity
Serving our customers is at the heart of our model. We have a global franchise model led by management who are specialists in their markets. This keeps us close to our customers, ensuring we can anticipate and meet their needs.

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### REVENUE
$4,904m

### OPERATING PROFIT
$863m

### TRADING PROFIT
$1,123m

### DIVIDEND
$321m

### JOBS
16,000+

### EFFICIENCY SAVINGS
$60m

### PUBLISHED CLINICAL EVIDENCE
200+

### PRACTITIONER TRAINING INSTANCES
50,000+

### PHILANTHROPIC DONATIONS
$8m

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**Shareholders**
We have a progressive dividend policy and in respect of 2018 our shareholders benefited from a 3% increase in dividend. In addition, our shares rose 14% over the course of 2018.

**Patients**
Patients in more than 100 countries were treated with our products in 2018. We continued to widen access to our products, with 17% of revenue now coming from sales to the emerging markets.

**Customers**
We continued to expand treatment options available through R&D and acquisitions, published more than 200 pieces of clinical or economic evidence, and provided extensive professional development training.

**Employees**
6,000 employees engaged in the development of our new purpose and culture pillars which are guiding revised evaluation, diversity and development programmes.

**Communities**
We work in a sustainable, ethical and responsible manner, making $8m in cash and product donations in 2018.

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1 These non-IFRS financial measures are explained and reconciled to the most directly comparable financial measure prepared in accordance with IFRS on pages 194–198.
Our franchises

From 1 January 2019, we will serve our customers through three franchises

<table>
<thead>
<tr>
<th>Orthopaedics</th>
<th>Sports Medicine &amp; ENT</th>
<th>Advanced Wound Management</th>
</tr>
</thead>
<tbody>
<tr>
<td>Orthopaedics includes an innovative range of Hip and Knee Implants used to replace diseased, damaged or worn joints and Trauma products used to stabilise severe fractures and correct bone deformities.</td>
<td>Our Sports Medicine and Ear, Nose and Throat (ENT) businesses offer advanced products and instruments used to repair or remove soft tissue. They operate in growing markets where unmet clinical needs provide opportunities for procedural and technological innovation.</td>
<td>Our Advanced Wound Management portfolio provides a comprehensive set of products to meet broad and complex clinical needs, to help healthcare professionals get CLOSER TO ZERO human and economic consequences of wounds.</td>
</tr>
</tbody>
</table>
Orthopaedics

Proven products to enhance quality of life

Smith & Nephew’s Orthopaedics franchise includes an innovative range of Hip and Knee Implants used to replace diseased, damaged or worn joints, and Trauma products used to stabilise severe fractures, correct bone deformities, treat arthritis and heal soft tissue complications.

KNEE IMPLANTS

Every year more than two million patients receive total, partial or revision knee replacements worldwide.1 Smith & Nephew’s range of products for specialised knee replacement procedures include leading products for total, partial and patellofemoral joint resurfacing procedures. Customers and patients benefit from our unique technologies including our proprietary advanced bearing surface, VERILAST™, our robotics-assisted platform, NAVIO™ Surgical System, and our customised VISIONAIRE™ Patient-Matched Instrumentation.

Smith & Nephew’s JOURNEY™ II Total Knee Arthroplasty system is designed and demonstrated to replicate normal knee positions, shapes, and motions.2-8 The range includes bi-cruciate stabilised and cruciate retaining options, and the JOURNEY II XR, an innovative bi-cruciate retaining knee implant launched in 2018, which is designed to retain the anterior and posterior cruciate ligaments (ACL/PCL) and deliver normal perception of movement and muscle control.9

The LEGION™/GENESIS™ II Total Knee System is a comprehensive system designed to allow surgeons to address a wide range of knee procedures. It includes the LEGION Revision Knee System, designed to offer surgeons improved options to deal with the complexities associated with revision knee arthroplasty. These systems feature VERILAST Technology, our advanced bearing surface of OXINIUM® Oxidized Zirconium with highly cross-linked polyethylene. The LEGION Primary Knee with VERILAST Technology has been laboratory-tested for 45 million cycles of wear simulation, approximating 30 years of activity. While lab testing is not the same as clinical performance, the tests showed significant reduction in wear compared to conventional technologies.10

Our ANTHEM™ Total Knee System and ORTHOMATCH™ Universal Instrumentation Platform, launched in 2017, are designed to provide wider market access to affordable knee treatment. ANTHEM is tailored to meet the anatomical needs of patients from Asia, the Middle East, Africa and Latin America and the ORTHOMATCH instrumentation platform reduces weight, footprint and unnecessary cost without compromising on quality.11

The NAVIO Surgical System provides accuracy,12-20 flexibility and confidence utilising real-time imaging (without the need for a preoperative CT scan), hand-held robotics, a portable cart, and multiple partial and total knee implant options in an economically sound platform.21 NAVIO offers both partial and total knee options that include the first and only robotics-assisted bi-cruciate retaining knee procedure commercially available today. Additionally, our knee systems can utilise our VISIONAIRE Patient-Matched Instrumentation, whereby an MRI and X-Rays are used to create customised cutting guides designed to allow the surgeon to achieve optimal alignment of the new implant.12

HIP IMPLANTS

Smith & Nephew’s Hip Implants franchise offers a range of specialist products for reconstruction of the hip joint. This may be necessary due to conditions such as arthritis causing persistent pain and/or as a result of hip fracture. Every year more than two million patients worldwide undergo total, resurfacing and revision hip replacement procedures.1

Smith & Nephew has developed a range of primary hip systems. Core systems include the ANTHOLOGY® Hip System, SYNERGY® Hip System and the POLAR3™ Total Hip Solution. This diversity exemplifies our commitment to providing surgeons with implant and instrumentation options that meet the specific demands of their patients and preferred surgical approach, most notably the direct anterior or posterolateral approach. We also market the BIRMINGHAM HIP® Resurfacing (BHR) System, an important option for surgeons treating suitable patients.
Orthopaedics

Smith & Nephew’s portfolio also includes the REDAPT™ Revision Hip System. The need to perform a revision can occur for a variety of reasons including infection, dislocation, or failure of the implants to achieve biologic fixation. REDAPT is designed to turn such complex hip revisions into efficient, reproducible surgeries, allowing surgeons to effectively recreate a patient’s unique functionality, while quickly and easily addressing issues such as poor bone quality.25

The REDAPT Fully Porous Acetabular Cup with CONCELOC® Technology is designed to allow ingrowth through an additive, or 3D printing, manufacturing process which produces a porous implant that mimics the structure of cancellous bone. The 3D printing method allows for complex design geometries that would be difficult, expensive or impossible to achieve with traditional manufacturing methods.24

TRAUMA

In Trauma, the TRIGEN™ INTERTAN™ hip fracture system allows patients to experience lower risk of implant failure and re-operation, faster time to fracture union, and a high return to pre-fracture status.25

The EVOS® Plate and Screw System is a stainless steel, highly versatile system with a multitude of plate geometries and longer screw lengths than standard mini fragment systems. The EVOS Small Fragment system for lower extremity fractures and general trauma utilisation features more points of fixation and greater breadth of plate options.

For extremities and limb restoration, our range includes the TAYLOR SPATIAL FRAME® External Fixator as well as plates, screws, arthroscopes, instrumentation, resection and suture anchor products for foot and ankle and hand and wrist repair as well as INVISIKNOT®, a unique syndesmosis fixation device for the ankle.

References

1. 2018 Smith & Nephew Market Model.
18. Mitra R. Poster presented at: World Arthroplasty Congress; April 2018; Italy.
23. Smith & Nephew 10864 V1 REDAPT Revision Acetabular Augment Design Rationale 0718.

* The LEGION Primary CR Knee System completed 45 million cycles of in vitro simulated wear testing, which is an estimate of 30 years of activity. Other LEGION VERILAST Primary Knee Systems underwent similar lab testing comparable to industry standards. The results of in vitro wear simulation testing have not been proven to quantitatively predict clinical wear performance. Also, a reduction in total polyethylene wear volume or wear rate alone may not result in improved clinical outcomes as wear particle size and morphology are also critical factors in the evaluation of the potential for wear mediated osteolysis and associated aseptic implant loosening. Particle size and morphology were not evaluated as part of the testing.

** These non-IFRS financial measures are explained and reconciled to the most directly comparable financial measure prepared in accordance with IFRS on pages 194-198.
The POLARSTEM and R3 Total Hip Solution has the best survivorship figures of any total hip construct at seven years according to the world's largest national joint registry.26
Technology to improve healthcare

Smith & Nephew’s Sports Medicine and Ear, Nose and Throat (‘ENT’) franchise operates in growing markets where unmet clinical needs provide opportunities for procedural and technological innovation.

SPORTS MEDICINE JOINT REPAIR
In Sports Medicine Joint Repair, our technologies, instruments and implants enable surgeons to perform minimally invasive surgery of the joints, including the repair of soft tissue injuries and degenerative conditions of the shoulder, knee, hip and small joints.

For shoulder repair, we market products primarily for Rotator Cuff Repair (RCRI) and instability repair, two of the most commonly performed sports medicine procedures. Our key shoulder repair products include a variety of suture anchors, such as HEALICOIL® Suture Anchors featuring open-architecture design and SUTUREFIX® and Q-FIX® All-Suture Anchors, suture passers such as FIRSTPASS® ST, and ULTRABRAID® and ULTRATAPE Sutures. All these products can be used together or in conjunction with other existing products from the Smith & Nephew portfolio in a breadth of our comprehensive solutions for shoulder repair.

Enhancing our RCR portfolio, the REGENETEN® Bioinductive Implant, acquired in 2017, is a breakthrough technology and technique that balances biomechanics and biology to enhance the body’s natural healing response, helping tendons heal by inducing growth of new tendon-like tissue.1,5

Rotator cuff disease is a significant and costly problem3,16,17 that causes ongoing pain and limits patients’ mobility.18 The REGENETEN Bioinductive Implant stimulates the body’s natural healing response to support new tendon growth and disrupt disease progression.3,19

Brad Cannon
President of Sports Medicine & ENT

18 Strategic report

1-3 Strategic report Smith & Nephew Annual Report 2018

OUR FRANCHISES continued
The REGENETEN implant is highly complementary to our Sports Medicine portfolio, especially for enhancing a broad spectrum of rotator cuff repairs, serving an unmet clinical need and providing a compelling new treatment option for our customers.

In knee repair, the FAST-FIX family of Meniscal Repair Systems, FIRSTPASS MINI Suture Passer, and the ACUFEX Meniscal Root Repair System increase the number of meniscal injuries we can help surgeons address. For ligaments, the ENDBUTTON and ULTRABUTTON fixed and adjustable loop devices, BIOSURE interference screws, and the new ACUFEX EXTRA-ARTICULAR Reconstruction Guide System give surgeons multiple tools for performing single and complex ligament repairs. Outside the United States, the CARGEL Bioscaffold can be used in conjunction with microfracture to repair articular cartilage. With these products, we provide a unique package of solutions used by surgeons to help them restore knee function for their patients.

In December 2018, we announced the acquisition of Ceterix Orthopaedics, Inc., the developer of the NovoStitch Pro Meniscal Repair System. This unique device addresses complex meniscal tear patterns not adequately served by other repair systems and is highly complementary to Smith & Nephew’s leading FAST-FIX 360 Meniscal Repair System. The acquisition completed on 22 January 2019.

The Smith & Nephew joint repair portfolio includes implants made from a variety of biocompatible materials, including next-generation anchors made of soft, all-suture material and REGENESORB, an advanced biocomposite. For example, the Q-FIX All-Suture Anchor is ideal for a variety of arthroscopic shoulder and hip repairs, offering fixation performance superior to commonly used all-suture anchors and traditional anchors. The SUTUREFIX ULTRA All-Suture Anchor is an attractive option for procedures in which anatomic space is very limited, while still delivering high fixation strength. Implants made from REGENESORB, including versions of the HEALICOIL Suture Anchor for shoulder repair and BIOSURE Interference Screw for knee repair, have been shown to be absorbed and replaced by bone within 24 months in pre-clinical studies.

**ARTHROSCOPIC ENABLING TECHNOLOGIES (AET)**

AET products are often used in conjunction with products from Sports Medicine Joint Repair. AET includes high definition imaging solutions, industry leading energy-based and mechanical resection platforms, and fluid management and access technologies. Our platforms work in concert to facilitate access to various joint spaces, visualise the patient’s anatomy, ressect degenerated or damaged tissue and prepare the joint for a soft tissue repair.

The WEREWOLF and QUANTUM 2® COBLATION® Controllers, which are used with a wide range of high performance COBLATION radio frequency (RF) wands, enable surgeons to remove soft tissue precisely and control bleeding in a variety of arthroscopic procedures. WEREWOLF, our latest advance in COBLATION Technology, and the FLOW 50® Wand have demonstrated faster patient recovery and better long-term pain control and safety in knee procedures. The WEREWOLF and QUANTUM 2 Controllers and their associated wands carry broad indications across Sports Medicine.

The LENS Integrated Visualisation System provides outstanding image quality and functionality in a simple three-in-one console (CCU, LED Light Source and Image Management System), camera head and iPad application. Our DYONICS’ shaver blades provide superior resection due to their sharpness and reduced clogging with their debris evacuation capabilities. GOFO® and Double® Pump Fluid Management Systems facilitate surgical access by expanding the joint space, providing haemostasis, and maintaining the saline environment necessary to perform arthroscopic procedures.

**EAR, NOSE & THROAT (ENT)**

In ENT, our COBLATION Technology has been used to remove tonsils and adenoids for over 15 years and is preferred by surgeons and patients for its ability to remove tissue at low temperatures with minimal damage to surrounding tissue. COBLATION Technology is also marketed for use in turbinate and laryngeal procedures. Our RAPID RHINO® Carboxymethylcellulose (CMC) Technology is featured in both dissolvable and removable nasal and sinus dressings and epistaxis treatment products.

When mixed with water, CMC forms a cushioning gel that naturally drains from the body after several days and supports healing by maintaining a moist physical environment.

**OUR PERFORMANCE IN 2018**

<table>
<thead>
<tr>
<th>Sector</th>
<th>Revenue</th>
<th>Reported growth</th>
<th>Underlying growth**</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sports Medicine Joint Repair</td>
<td>$697m</td>
<td>11%</td>
<td>8%</td>
</tr>
<tr>
<td>AET</td>
<td>$600m</td>
<td>-2%</td>
<td>-3%</td>
</tr>
<tr>
<td>Other Surgical Business**</td>
<td>$209m</td>
<td>10%</td>
<td>10%</td>
</tr>
</tbody>
</table>

In 2018, strong growth in Sports Medicine Joint Repair franchise was driven by our shoulder repair portfolio. Within this, the recently acquired REGENETEN Bioinductive Implant for rotator cuff repair delivered more than 130% growth, performing ahead of expectations. AET performance was held back by continued softness in mechanical and legacy radio-frequency resection. We expect the launch of the FLOW 90° COBLATION® wand for shoulder in the first half of 2019 to support better growth.

Other Surgical Businesses double-digit growth reflects strong demand for our robotic NAVIO Surgical System from both the Established and Emerging markets.

**References**


**FDA cleared for use in the knee on all soft tissue types**
**These non-IRS financial measures are explained and reconciled to the most directly comparable financial measure prepared in accordance with IFRS on pages 194–198.***

***Includes ENT and NAVIO robotics system.
ADVANCED WOUND MANAGEMENT

Because of the breadth and depth of our portfolio we are uniquely positioned to support customers who follow best practice guidelines, including managing wounds with T.I.M.E.

T.I.M.E. stands for Tissue non-viable, Infection and/or Inflammation, Moisture imbalance, and Edge of wound non-advancing. These represent critical barriers of wound healing. T.I.M.E. was first established as a concept for best practice wound management in 2003 by a panel of world leading experts, and has since been widely adopted around the world, becoming a staple reference framework for routine clinical practice.

We use T.I.M.E. to help our customers navigate the complexity of product choices they face based on which clinical goal they may have, and we also use it to guide our own new product and programme development, as well as life cycle management, to ensure we remain relevant to the evolving clinical needs.

Having supported T.I.M.E. since its inception, at Smith & Nephew we are uniquely positioned to provide customers with differentiated and effective products via our Advanced Wound Care (AWC), Advanced Wound Devices (AWD) and Advanced Wound Bioactives (AWB) portfolio across each T.I.M.E.-based clinical need.

ADVANCED WOUND CARE (AWC)

Our AWC range covers several segments aimed at helping improve outcomes in the Infection and Moisture balance clinical goals of T.I.M.E.

In infection management, our silver-based dressings (ACTICOAT™, DURAFIBER Ag® and ALLEVYN™ Ag) provide clinicians with a range of solutions to address individual patient needs in managing wound infection. ACTICOAT, for instance, is a fast-acting, highly effective antimicrobial for serious infection on a wide range of wounds. Our Cadexomer iodine based IODOSORB® dressing is indicated clinically relevant in vitro tests, animal biofilm models and in clinical practice.

In exudate (or moisture) management our products are designed to respond to varying levels of wound exudate providing appropriate evaporation properties to promote an optimal wound healing environment. This helps patients get on with their lives as well as lowering costs for materials and nursing time by reducing unnecessary dressing changes. Our key growth brand in this space is the ALLEVYN range with two focus variants, ALLEVYN Gentle Border dressing (versatile and adaptable, so suitable for a wide variety of chronic and acute wounds) and ALLEVYN LIFE dressing (our most advanced dressing, uniquely differentiated by its distinct quadrilobe shape which lasts for up to two times longer than any other dressing). The ALLEVYN range was extended in 2018 through the launch of ALLEVYN LIFE Non-Bordered to ensure the portfolio continues to meet broad needs.

The rest of our AWC range includes our film and post-operative dressings, skincare products and gels. Leading brands include OPSITE™ dressings, IV3000™, PROSHIELD® and SECURA®.

ADVANCED WOUND BIOACTIVES (AWB)

Our AWB portfolio covers key product segments aimed at helping improve outcomes in the Tissue viability and wound Edge advancement clinical goals of T.I.M.E.

In this part of our business we focus on the commercialisation of topical biologics and a skin substitute that provide a unique approach to debridement, dermal repair, and tissue regeneration.

Our portfolio includes Collagenase SANTYL® Ointment, OASIS® Wound Matrix and OASIS ULTRA Tri-Layer Matrix (a naturally-derived, extracellular matrix replacement product indicated for the management of both chronic and traumatic wounds) and REGRANEX® (becaplermin) Gel 0.01%.

Our most significant product by sales in this segment is SANTYL Ointment, the only FDA-approved biologic enzymatic debriding agent for chronic dermal ulcers and severe burns. SANTYL plays an integral role in debriding chronic dermal ulcers and severely burned areas.
The UK’s National Institute for Health and Care Excellence (NICE) issued a Medtech innovation briefing on the prophylactic use of PICO which highlighted its potential to be more effective at preventing surgical site infections than standard surgical dressings. This is the only such briefing published by NICE on an NPWT device for preventing such complications.
ADVANCED WOUND DEVICES (AWD)

Our AWD portfolio covers key product segments aimed at helping improve outcomes in the Tissue viability, Moisture balance, and wound Edge advancement clinical goals of T.I.M.E.

In the NPWT segment, the PICO® Single Use Negative Pressure Wound Therapy System (sNPWT) brings the effectiveness of traditional NPWT in a modern, small portable system.

It is designed for both open wounds and closed incisions, and leverages our proprietary AIRLOCK™ dressing technology.

During the year, we extended the PICO range with the introduction of two new models.

PICO 7 delivers a more efficient vacuum and superior leak management than the previous version, includes an industry-first dressing-full indicator, which is intended to help reduce unnecessary dressing changes and wastage, and is over 25% quieter than the previous version.

PICO 7Y, launched in Europe in 2018, is the first sNPWT system to include an innovative integrated Y connector enabling the utilisation of two dressings concurrently from one pump, in practice allowing for two wounds to be addressed at the same time, thereby potentially reducing cost.

The PICO evidence base continued to grow, validating the patient and provider benefits of the technology, with the publication of key studies in multiple indications including orthopaedics, vascular, plastics, OBGYN, breast reconstruction and chronic wounds.

With RENASYS® NPWT system, our strategy is to simplify the delivery of NPWT, combining the advantages of PICO with the simplicity and power of RENASYS TOUCH, an intuitive touchscreen traditional NPWT device delivering advanced features to manage large, highly exuding wounds.

This franchise also includes the VERSAJET® Hydrosurgery system, a surgical debridement device used by surgeons to excise and evacuate non-viable tissue, bacteria and contaminants from wounds, burns and soft tissue injuries.

OUR PERFORMANCE IN 2018

<table>
<thead>
<tr>
<th>Product Line</th>
<th>Revenue</th>
<th>Reported growth</th>
<th>Underlying growth</th>
</tr>
</thead>
<tbody>
<tr>
<td>Advanced Wound Care</td>
<td>$740m</td>
<td>3%</td>
<td>1%</td>
</tr>
<tr>
<td>Advanced Wound Bioactives</td>
<td>$320m</td>
<td>-6%</td>
<td>-6%</td>
</tr>
<tr>
<td>Advanced Wound Devices</td>
<td>$215m</td>
<td>10%</td>
<td>9%</td>
</tr>
</tbody>
</table>

In 2018, performance in Advanced Wound Care included good growth in the US, led by ALLEVYN LIFE and our pressure ulcer prevention strategy, offset by softness in some European countries.

In Advanced Wound Bioactives, performance from SANTYL, our largest product, was weaker than the previous year as volumes came under pressure. Following review of two large safety studies, the FDA approved the removal of the boxed warning from REGRANEX, and we will relaunch this product in early 2019.

Advanced Wound Devices delivered strong growth led by demand for our PICO sNPWT, which benefited from the launch of two new models in 2018.

REFERENCES

9. SANTYL is indicated for chronic dermal ulcers and severely burned areas. Occasionally, slight transient erythema has been noted in surrounding tissue when applied outside the wound. One case of systemic hypersensitivity has been reported after 1 year of use with collagenase and cortisone. Use of SANTYL Ointment should be terminated when debridement is complete and granulation tissue is well-established. See full prescribing information for more details.
24. Fortee, et al. EWMA; 2018; Poland.

* These non-IFRS financial measures are explained and reconciled to the most directly comparable financial measure prepared in accordance with IFRS on pages 194-198.
Our resources

The resources we need to deliver our products and serve our customers

<table>
<thead>
<tr>
<th>Our people &amp; culture</th>
<th>24</th>
</tr>
</thead>
<tbody>
<tr>
<td>Ethics &amp; compliance</td>
<td>26</td>
</tr>
<tr>
<td>Sales &amp; marketing</td>
<td>27</td>
</tr>
<tr>
<td>Manufacturing &amp; quality</td>
<td>28</td>
</tr>
<tr>
<td>Medical education</td>
<td>29</td>
</tr>
<tr>
<td>Research &amp; development</td>
<td>30</td>
</tr>
<tr>
<td>Sustainability</td>
<td>32</td>
</tr>
</tbody>
</table>
Our people & culture

A unifying purpose and culture of care, collaboration and courage to win

Smith & Nephew has a proud history of more than 160 years of improving health around the world. Whilst we have grown significantly from our beginnings as a small family pharmacy in Hull, England, our caring spirit has remained the same.

In 2018, led by our new management team, Smith & Nephew began the work to create a culture that, whilst rooted in caring, was also clearly aligned on a unifying purpose and culture of collaboration and courage to win.

Throughout the year, in addition to gauging our progress against our framework of Great Place to Work (GPTW), we engaged employees in a review of our existing culture and future aspirations. GPTW Pulse surveys were conducted in four of our major markets – US, China, UK and Australia/New Zealand – with an overall response rate of 75% and China again receiving country-level recognition. GPTW recognition was also received during the year in Austria, Ireland, Poland and the UAE.

In addition, we conducted a voluntary feedback survey and subsequent focus groups with participation from nearly 40% of the workforce to review our company culture. Together, this input formed the basis for a new purpose, Life Unlimited (see page 8), and our culture pillars of Care, Collaboration and Courage. These pillars represent the best of Smith & Nephew today, as well as what we aspire to be in the future.

CARE

Our culture pillar of Care means that we show empathy and understanding for each other, our customers and patients. We step into our customers’ shoes, anticipate their needs and deliver the highest levels of innovation and service.

We strive to have the best understanding of the patients whom we ultimately serve, and we develop our products with them in mind. And, our passion for what we do drives us to continuously improve and expand the positive impact that we have on the world.

In 2018, our people displayed this culture in numerous ways, including charitable donations and sponsorships of more than 50 organisations in the communities where we live and work. This extends to support of our own employees in times of need.

For example, in 2018, US employees who were displaced from their homes due to a gas pipeline explosion were provided lodging or heaters until their power returned.

We encourage all our employees to volunteer their time and talents by providing paid time for volunteer efforts. Many functions structured their team building activities around group volunteering opportunities such as Make a Wish Foundation events and Habitat for Humanity.

By continuously improving our own performance, we can increase our positive influence on the world. To encourage this, we offer advancement and development opportunities for our employees. Employee advancement is merit-based, reflecting performance as well as demonstration of our newly created Winning Behaviours, which underpin our culture pillars and replace our previous core competencies.

Each year Smith & Nephew conducts a comprehensive global development and capability review process to identify high potential employees and ensure they have well defined career development plans.

Employees are provided with opportunities to develop their skills and career through new assignments and on the job experiences. In addition, succession plans are in place for key executive roles and other critical positions across our business.

COLLABORATION

Our culture pillar of Collaboration means we work together as a team, based on mutual trust and respect. Through transparent and respectful communication, we are motivated by a shared purpose and understand the impact of our individual contributions on our collective goals. And, by encouraging different perspectives and leveraging our global experiences we achieve the best outcomes.

In 2018, we broadened our quarterly business performance communications to include live global webcasts featuring Namal Nawana and members of his executive team. These included an open question and answer dialogue with employees around the world in real-time. The feedback has been tremendously positive, increasing transparency and supporting our shared purpose.

We provide peer-to-peer recognition to celebrate achievements or just say ‘thank you’ via our Going the Extra Mile (GEM) programme. Awards range from simple notes to appreciation through substantial monetary awards.

We are committed to employment practices based on equal opportunities, regardless of colour, creed, race, national origin, sex, age, marital status, sexual orientation, or physical or intellectual disability. We believe a person’s ability to perform essential functions of a job is the only relevant criteria.
In 2018, an internal evaluation showed that those teams with greater diversity achieved better results. The work also revealed that our people understand why valuing difference is important and our teams benefit from high levels of trust and respect.

We have raised awareness of preventing unconscious biases through our management and Human Resources training globally, carrying out a Talent Acquisition Diversity and Inclusion Masterclass. We also conducted inclusion workshops at the 2018 Managing Directors’ Meeting and numerous regional leadership business meetings.

We stepped-up our efforts to accelerate the development of women in our business. We have extended our Elevate women’s leadership development programme, including nearly 300 participants in 2018. We also attended the 2018 Conference of the Society of Women Engineers, to generate further awareness and recruit female talent in the science and engineering fields. In addition, in 2018, we added another female leader to our executive team.

**COURAGE**

Our culture pillar of Courage is about continuous learning, innovation and accountability. By staying curious, thinking big and having the humility to challenge our conventional ways of thinking, we push the boundaries of our industry. Fostering an entrepreneurial, can-do attitude we look for solutions and achieve them through talent and force of will. And, with a growth mindset, we have the capability and confidence to win, and we do so with integrity and the highest ethical standards. We start each year by setting clear and measurable objectives with a clear strategy communicated Company-wide.

The strategic imperatives and annual targets form the basis of individual objectives of every employee in the Company according to his or her role. Through this process, each employee can clearly see how their efforts contribute to the overall success of the business, which drives execution, accountability and engagement.

We continued to provide opportunities for all levels of the organisation to strengthen their skills through development programmes including Pioneer, Edge and Continuous Learning Journey. These programmes consistently received positive feedback from participants.

Smith & Nephew’s compensation also supports high-performance and accountability. Employees are compensated based on sustained performance that helps deliver timely and tangible results to drive the business forward and support our culture.

Having a robust compensation framework is vital as we seek to recruit high calibre people. By following this philosophy we have found that we not only attract, retain, and motivate talent, but it also helps drive better business results and provides an equitable work environment. We are Living Wage Accredited in the UK, voluntarily paying above the government required minimum as we believe employees should receive fair compensation for the work they do.

### NUMBER OF EMPLOYEES’ 2018

<table>
<thead>
<tr>
<th>Total employees</th>
<th>Senior managers(^2) and above</th>
<th>Board of Directors</th>
</tr>
</thead>
<tbody>
<tr>
<td>16,377</td>
<td>788</td>
<td>12</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Male</th>
<th>Female</th>
<th>Male</th>
<th>Female</th>
<th>Male</th>
<th>Female</th>
</tr>
</thead>
<tbody>
<tr>
<td>58%</td>
<td>42%</td>
<td>73%</td>
<td>27%</td>
<td>75%</td>
<td>25%</td>
</tr>
</tbody>
</table>

\(^1\) Number of employees at 31 December 2018 including part time employees and employees on leave of absence.

\(^2\) Senior managers and above include all employees classed as Directors, Senior Directors, Vice Presidents, Executive Officers and includes all statutory directors and Directors of our subsidiary companies.

**REDEFINING OUR CULTURE**

6,000 employees participated in our programme to define our new purpose and culture pillars. We used feedback surveys and ran workshops at our sites across the world, including in Japan.

**SUPPORTING WOMEN**

We encourage women to follow careers in STEM. Our Society of Women Engineers (SWE) chapter is thriving, with more than 110 members. We had a major presence at the 2018 SWE Conference, recruiting for talented new graduate engineers.

For more information about how we are putting people first, download our Sustainability Report from our website.
Ethics & compliance

Smith & Nephew has a strong reputation for integrity and ethical behaviour

CODE OF CONDUCT AND BUSINESS PRINCIPLES

Smith & Nephew earns trust with customers, healthcare professionals, government authorities, patients and the public by acting in an honest and fair manner in all aspects of its operations.

We expect the same from those with whom we do business, including vendors who provide us with products and services and distributors and independent agents that sell our products. Our Code of Conduct and Business Principles governs the way we operate to achieve these objectives.

Smith & Nephew takes into account ethical, social, environmental, legal and financial considerations as part of its operating methods. We have a robust whistle-blowing system in all jurisdictions in which we operate which is benchmarked against industry metrics. We are committed to upholding the promise we make in our Code of Conduct to not retaliate against anyone who makes a report in good faith.

GLOBAL COMPLIANCE PROGRAMME

Smith & Nephew has implemented what we believe to be a world-class Global Compliance Programme that helps our businesses comply with laws and regulations.

This includes: Board and executive oversight committees; global policies and procedures; on-boarding and annual training for employees and managers; training for distributors and agents and higher-risk vendors; monitoring and auditing processes; reporting channels and employee-recognition for demonstrating our values in their everyday work.

We provide resources and tools to guide employees to make decisions that comply with the law, local industry codes and our Code of Conduct. We review and approve significant interactions with healthcare professionals or government officials in advance. We regularly assess existing and emerging risks in the countries in which we operate.

We assess the compliance controls in Smith & Nephew’s businesses. We conduct audits, supported by data analytics, with central and local monitoring. We review the issues our testing generates to identify patterns.

New distributors and other higher-risk third parties are subject to screening and are contractually obligated to comply with applicable laws and our Code of Conduct. Compliance training and certifications are included in this process, including guidelines for those who need to enter the operating room when acting on our behalf.

Senior leaders, including all Vice Presidents and above, are required to complete an annual certification to the Chief Executive Officer to confirm the implementation of required policies. Managers and employees make an annual compliance certification and conflict of interest disclosure.

We constantly seek new ways to enhance our Compliance Programme. New measures in 2018 included expanding the compliance ambassador process where selected sales staff serve as compliance contact for their peers for some training and questions, successfully completing a pilot for an enhanced root cause analysis methodology for recurring issues and implementing additional processes and training on data privacy.

AN ETHICAL EMPLOYER

We recruit, employ and promote employees on the sole basis of the qualifications and abilities needed for the work to be performed. We do not tolerate discrimination on any grounds and provide equal opportunity based on merit.

We do not use any form of forced, compulsory or child labour. We support the Universal Declaration of Human Rights of the United Nations. This means we respect the human rights, dignity and privacy of the individual and the right of employees to freedom of association, freedom of expression and the right to be heard.

As a global medical technology business, Smith & Nephew recognises that we have a responsibility to take a robust approach to preventing slavery and human trafficking. Smith & Nephew is committed to preventing slavery and human trafficking in its corporate activities, and its supply chains. Our full policy on preventing slavery is available on our website.
Sales & marketing

We put customers at the heart of our commercial model

Our customers are the providers of medical and surgical treatments and services in over 100 countries worldwide, ranging from orthopaedic surgeons to wound care nurses, general practitioners and other clinicians, but increasingly also economic stakeholders.

These include purchasing professionals in hospitals, healthcare insurers, materials managers and others.

We serve these customers through our sales force and other channels. Our sales representatives are highly trained and skilled individuals. Becoming a sales representative requires intense training, including passing a strict certification programme.

Depending on their area of specialism, representatives in our surgical businesses must be able to demonstrate a detailed knowledge of all the surgical instruments used to implant a device, or have specific understanding of the various surgical techniques a customer might use.

In our Advanced Wound Management business, sales representatives must have a detailed understanding of how patients live with wounds and how clinicians seek to prevent and treat them, as well as deep knowledge of the clinical and economic benefits of using our products within treatment protocols.

Once a sales representative is certified, they typically spend the majority of their time working directly with and supporting customers, or identifying and contacting new customers. They help to provide in-hospital support to aid in the safe and effective use of our range of advanced medical technologies and techniques.

In 2018, we began the implementation of a global franchise structure with dedicated presidents of Orthopaedics, Sports Medicine & ENT and Advanced Wound Management to direct and support our customer facing activities. This new structure will replace our regional selling model in 2019.

Under the new structure, each president will lead their franchise with global upstream marketing responsibility and full commercial responsibility for their franchise in the US. They will also lead one or more shared global commercial support teams, in the critical areas of professional education, sales training and healthcare economics. In addition, the president of Sports Medicine & ENT has commercial responsibility for Latin America and Canada.

Outside of the Americas, our commercial activities will be run through two regions – Europe, Middle East and Africa, and Asia Pacific – each under a president. Under these presidents will be country clusters, a group of countries, based on geographic proximity, critical mass of revenue, and similar go-to-market strategies. They will be led by a single managing director and have business unit leads for each franchise.

This structure will reduce complexity and take out administrative costs, and importantly will bring us closer to our customers.

In 2018, we began to make these changes while keeping stability in our selling and customer-facing organisations.
Manufacturing & quality

Efficiently delivering products of the highest quality

Smith & Nephew takes great pride in its expertise in manufacturing products to the highest quality and ensuring they reach our customers in a timely manner.

We operate manufacturing facilities in nine countries across the globe and have central distribution facilities in the US, Europe and Asia. Products are shipped to individual country locations to meet customer requirements.

Manufacturing is a dynamic process and our Global Operations leadership team is focused on successfully supporting delivery of the Group’s strategic priorities by ensuring our footprint and expertise is ready to respond to geographical growth, new product development, greater external regulatory scrutiny and the commercial pressure to be ever more efficient.

Products for our Orthopaedics franchise are made in sites in Memphis (Tennessee, US), Aarau (Switzerland), Tuttingen (Germany), Beijing (China), Warwick (UK), Puschino (Russia) and Devrukh (India). Memphis is our largest location and is home to the design and manufacturing process of the OXINIUM Oxidised Zirconium, a patented metal alloy available for many of our knee and hip implant systems as part of our VERILAST technology.

In Sports Medicine Joint Repair, products are manufactured at our Mansfield (Massachusetts, US) and Alajuela (Costa Rica) facilities.

The majority of our Advanced Wound Management products are manufactured at our facilities in Hull (UK), Suzhou (China) and Curacao. We have also invested in a new facility in Fort Worth, Texas, to support our Advanced Wound Bioactives franchise. Our Oklahoma City facility in the US produces and services electro/mechanical capital equipment as well as single-use sterile devices and also assembles some of our NPWT devices using components from third parties.

We procure raw materials, components, finished products and packaging materials from suppliers in various countries. These include metal forgings and castings for orthopaedic products, optical and electronic sub-components for Sports Medicine Joint Repair products, active ingredients and semi-finished goods for Advanced Wound Management as well as packaging materials across all product ranges. Suppliers are selected, and standardised contracts negotiated, by a centralised procurement team wherever possible, with a view to ensuring value for money based on the total spend across the Group. On an ongoing basis, we work closely with our key suppliers to ensure high quality, delivery performance and continuity of supply.

We outsource certain parts of our manufacturing processes where necessary to obtain specialised expertise or to lower cost without undue risk to our intellectual property. Suppliers of outsourced products and services are selected based on their ability to deliver products and services to our specification, and adhere to and maintain an appropriate quality system. Our specialist teams work with and monitor suppliers through on-site assessments and performance audits to ensure the required levels of quality, service and delivery.

Our Global Supply Chain team ensures that our products reach our internal and external customers where and when they are needed, in a compliant and efficient manner. We operate main holding warehouses for surgical products, one in each of Memphis (TN, US), Columbus (OH, US), Baar (Switzerland) and Singapore. These facilities consolidate and ship to local country and distributor facilities. Our distribution hubs for Advanced Wound Management products are located in Neunkirchen (Germany), Derby (UK) and Lawrenceville (Georgia, US).

QUALITY AND REGULATORY AFFAIRS

Quality is of paramount importance to Smith & Nephew. In 2018, we restructured the global Quality and Regulatory Affairs function to ensure consistent high standards across the Group. This function is led by the Chief Quality and Regulatory Affairs Officer, a new role reporting directly to the Chief Executive Officer.

Requirements of global regulatory agencies have become more stringent in recent years and we expect them to continue to do so. The team is leading a major Group-wide programme to prepare for implementation of the European Union (EU) Medical Devices Regulation (MDR), which came into force in May 2017, with a three-year transition period until May 2020. The regulation includes new requirements for the manufacture, supply and sale of all CE marked products sold in Europe and requires the re-registration of all medical devices, regardless of where they are manufactured.

Quality and Regulatory Affairs has also provided leadership in preparing the Group for Brexit, which has required the management of changes to our European Authorised Representative strategy and Notified Body relationships. Finally, the team continued to support the expansion of our portfolio globally through the registration of new products and existing products in new markets.
Medical education

Supporting the safe and effective use of our products

Smith & Nephew is dedicated to helping healthcare professionals improve the quality of care for patients. We are proud to support the development of surgeons and nurses by providing skills training and education on our products and techniques.

In 2018, we provided more than 30,000 instances of training to surgeons through our Smith & Nephew training centres in the US, UK and China, as well as running many courses at third party centres around the world. In 2018, we opened a new surgical training centre in Phoenix (Arizona) to bring professional development and skills training to customers, primarily in the West and Southwest of the US, complementing Smith & Nephew’s existing US facilities in Memphis (Tennessee), Andover (Massachusetts), Austin (Texas) and Plymouth (Minnesota).

Working under expert guidance, attendees learn new techniques and refine skills, to ensure the safe and effective use of our products. These courses are attended by residents, fellows and practising surgeons who work together to review, discuss and train on current and forward-looking surgical techniques in their areas of clinical expertise. Our courses help up-and-coming surgeons develop trust and gain the experience and confidence necessary to become experts in their field.

Thousands of nurses receive face-to-face training from Smith & Nephew representatives every year, including attending courses at our centres, and through our representatives visiting them at their place of work. In 2018, more than 20,000 clinicians benefited from our specialist wound care education training courses.

In addition, we provide healthcare professionals our online resources such as the Global Wound Academy, The Wound Institute and, for surgeons, our Education and Evidence website. Recently we began utilizing innovative, digital technologies to accelerate the learning experience of surgeons. In 2018, we provided digital training on Smith & Nephew products and techniques to 225,000 healthcare professionals, a 25% increase over the prior year.

ECC ENDORSED BY ROYAL COLLEGE OF SURGEONS

In 2018, Smith & Nephew’s Expert Connect Centre (ECC) in Watford, UK became the first commercial surgical training facility in Europe to be accredited by the Royal College of Surgeons. The recognition enables delegates to receive Continuing Professional Development (CPD) points when attending Smith & Nephew sessions, demonstrating their commitment to developing their surgical skills.
Research & development

We are increasing our investment in new products

Smith & Nephew's global Research & Development (R&D) function supports the Group's strategic imperatives by delivering innovative system solutions that aim to improve clinical and healthcare economic outcomes. We do this in partnership with our customers, executing new product development and clinical programmes across the enterprise.

In 2018, we invested $246 million in R&D, equivalent to 5% of Group revenue. Over time, we are committed to increasing this investment, driven by the needs of the business to support sustainable growth. In 2018, we launched a number of major new products and publications with evidence of clinical and economic value. Our major new product launches included the full commercial release of the bi-cruciate retaining JOURNEY II XR total knee arthroplasty (TKA) system, updates and extensions to our REDAPT Revision Hip System, the EVOS SMALL Plating System in Trauma, a suite of all-suture anchor shoulder repair systems in sports medicine and two new versions of our leading PICO Single Use Negative Pressure Wound Therapy System (NPWT).

We published more than 200 different abstracts and publications in peer-reviewed journals; a significant increase compared to previous years, and the result of increased investment in clinical studies. Highlights included 14 abstracts accepted at the World Arthroplasty Congress in Rome in April and the completion of one of the largest multi-centre retrospective patient cohorts ever studied with the JOURNEY II BCS TKA system. A number of studies highlighted how PICO can help manage scarring and surgical site infections. We were also successful in securing the NICE Medtech Innovation Briefing for PICO described on page 21.

OUR ENTERPRISE R&D OPERATING MODEL

Our enterprise R&D model provides governance and simple processes for new product development, starting with front end innovation and research, moving through new product development and launch, and ending with support of released products.

Project selection is critical; we focus on projects that will make a meaningful difference to our customers and their patients. This includes investing in incremental innovation to improve existing products. It also involves driving greater efficiency through innovation, potentially reducing our costs of goods. Finally, we aim to transform our business using disruptive technologies, services and business models.

Following project selection, the team challenges itself to execute flawlessly. This means developing the right product at the right cost and quality, and supported by clinical evidence. Our R&D experts in the UK, US, Europe, Singapore, China and India have extensive customer and sector knowledge, which is augmented by interaction with our marketing teams. Strict criteria are applied to ensure new products fulfill an unmet clinical need, have a strong commercial rationale, and are technologically feasible.

R&D works closely with the marketing, clinical, regulatory affairs, manufacturing and supply chain management teams to ensure we can produce new products to clinical, cost and time specifications.

We also continue to invest in scouting for new technologies, identifying complementary opportunities in our core and adjacent segments. In addition, we invest in small companies developing compelling technologies in our franchise areas through our incubation fund, and provide our expertise to help the development process, including supporting clinical studies, and typically secure preferred access to technology as it nears market readiness.

We work in partnership with academia. As an example, with the University of Hull we have created one of the world’s largest Wound Care Research Clusters and with Imperial College London we are developing enhanced surgical techniques relating to ligament function, biomechanics and soft tissue injuries of the knee.

We look to support our innovations with compelling evidence of clinical and economic value. The global R&D function includes our Clinical, Medical and Scientific Affairs (CMSA) teams, led by the Chief Medical Officer. This team ensures that, from conception, plans are developed to support product launches with the evidence increasingly required by clinicians, payers and regulators. Our products undergo clinical and health economic assessments both during their development and post-launch.

For 2019, we have a strong pipeline, with a number of important launches planned, and also expect to maintain the high cadence of clinical and economic evidence.
EXPANSIVE, USER FRIENDLY SYSTEM

The EVOS SMALL Plating System is indicated for fixation of small and long bone fractures in adults and children. It is an expansive, user-friendly system with multiple fixation options including non-locking, locking, variable-angle locking, optimised plate contours and screw trajectories as well as a low profile construct.

WIDENING OUR PORTFOLIO

The Q-FIX CURVED, Q-FIX MINI and SUTUREFIX CURVED All-Suture Anchor systems are important additions to Smith & Nephew’s sports medicine portfolio. For use in procedures where space is limited and the anatomy can be difficult to access, they are designed to aid in optimal suture anchor placement during drilling and insertion.

WORLD FIRST

The new PICO 7Y Single Use Negative Pressure Wound Therapy System (sNPWT) with AIRLOCK Technology is the first sNPWT system to include an innovative integrated Y extension. This enables the utilisation of two dressings concurrently from one pump, in practice allowing for two wounds to be addressed at the same time, thereby potentially reducing cost.

TREATING DIFFICULT REVISIONS

The REDAPT Revision Femoral System includes an additive, or 3D printed Fully Porous Acetabular Cup. With a number of new REDAPT Augments, to be used in conjunction with the porous shell, we are enabling surgeons to treat more difficult acetabular revisions.
Sustainability

Sustainability is better business

**SUSTAINABILITY IS AT THE CORE OF THE BUSINESS**
In 2016, we launched our Group Sustainability Strategy, setting out our aspirational goals and targets. The strategy is integrated with our Group Business Strategy. This ensures that the three main aspects of sustainability – economic prosperity, social responsibility and environmental stewardship – are tackled together.

This is a summary report of our sustainability activities and progress in 2018. Our annual Sustainability Report, published at the same time as this Annual Report, describes the Group Sustainability Strategy and its associated goals in more detail. It also specifies targets to move our performance towards these goals, and provides detailed information regarding the progress made during 2018. It is available on our website.

**GROUP SUSTAINABILITY STRATEGY**
Smith & Nephew has been and remains committed to working in a sustainable, ethical and responsible manner everywhere we do business. We are proud of our achievements over many years, as witnessed by our recurring inclusion in leading indices such as FTSE4Good and the Dow Jones Sustainability Index.

At the heart of the Group Sustainability Strategy are 10 long-term aspirational goals. These encompass all aspects of our business, and inform and drive our business strategy.

The Board has endorsed these and executive management is behind them. These goals are set out on the next page.

The Board has evaluated the social and environmental risks as part of their ongoing risk management duties and has concluded that none of these risks are material in the context of the Group as a whole.

We have set medium-term targets to 2020 which support our longer-term goals. These are discussed in more detail in our 2018 Sustainability Report.

2018 was a year in which we accelerated progress toward the achievement of our 2020 targets. We once again delivered improvements across our traditional areas of focus: employee health and safety, carbon emissions and water consumption. In addition, we deepened and broadened our understanding of our impacts in the areas of engagement in society, and labour practices. We deployed the social responsibility strategy developed in the previous year, positively contributing to employee engagement and supporting the communities in which we operate.

**SUSTAINABILITY VISION AND MISSION**
We envision a world in which healthcare professionals have access to the solutions they need to help patients restore their health, engage in society, enhance the environment and improve their wellbeing.

Our sustainability strategy aims to achieve this vision. It outlines the steps we take with a view to leading our industry in the development and use of products and services that:

- Satisfy unmet health needs and promote greater access to treatment;
- Offer easier, better, faster and more effective treatment, enabling productive engagement in society;
- Prioritise materials that are reused, remanufactured or recycled;
- Are manufactured using raw materials sourced from an environmentally and socially sound supply chain;
- Use natural resources efficiently;
- Are manufactured by processes that are not hazardous to people or the environment; and
- Implement the most sustainable product options.
OUR PERFORMANCE
Our 10 long-term aspirational goals

<table>
<thead>
<tr>
<th>2020 target</th>
<th>Performance to 31 December 2018</th>
</tr>
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<tbody>
<tr>
<td><strong>ZERO WORK-RELATED INJURIES AND ILLNESSES ACROSS THE VALUE CHAIN</strong></td>
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<tr>
<td>– 10% reduction in Total Injury Rate (TIR) from 2016 actual.</td>
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<tr>
<td><strong>WATER:</strong></td>
<td>Total water impacts of products and solutions balanced with local human and ecosystem needs.</td>
</tr>
<tr>
<td>– Water footprint available for products accounting for 75% of revenue and considerations embedded in new product development process. Total potable water consumption no higher than 2016 actual.</td>
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<tr>
<td><strong>WASTE:</strong></td>
<td>All materials are either shipped as part of product or returned for beneficial use.</td>
</tr>
<tr>
<td>– Total material efficiency estimated for products accounting for 75% of revenue and 80% or more of waste generated reused, recycled or recovered.</td>
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<tr>
<td><strong>CARBON:</strong></td>
<td>80% absolute reduction in total life cycle greenhouse gas emissions by 2050.</td>
</tr>
<tr>
<td>– Estimate total life cycle greenhouse gas emissions of products accounting for 75% of revenue.</td>
<td></td>
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<tr>
<td>– Total Scope 1 &amp; 2 greenhouse gas emissions reduced by 10% from 2016 actual.</td>
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<tr>
<td><strong>ETHICAL BUSINESS PRACTICES:</strong></td>
<td>All activities conducted in compliance with applicable International Labour Organization (ILO) conventions, involve no environmental degradation, and are free from corruption.</td>
</tr>
<tr>
<td>– Labour practices throughout the supply chain associated with products accounting for 75% of revenue compliant with applicable ILO conventions.</td>
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<tr>
<td><strong>ZERO PRODUCT-RELATED AND SERVICE-RELATED PATIENT INJURIES</strong></td>
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<tr>
<td>– Robust system in place to detect, record, investigate and eliminate root cause of product and service-related patient injuries.</td>
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<tr>
<td><strong>ROBUST SOCIAL RESPONSIBILITY PROGRAMMES</strong> that contribute to the attraction and retention of top talent.</td>
<td></td>
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<tr>
<td>– Social responsibility strategy which aligns philanthropy, employee volunteering and wellness to the business strategy.</td>
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</tr>
<tr>
<td><strong>PRODUCTS AND SERVICES</strong> are aligned to market economic, social and environmental expectations and anticipate future market conditions.</td>
<td></td>
</tr>
<tr>
<td>– Sustainability attributes described for products accounting for 75% of revenue. Robust emphasis on sustainability attributes of new products/services in place.</td>
<td></td>
</tr>
<tr>
<td><strong>STRATEGIC RISKS AND OPPORTUNITIES</strong> are understood and business activities are aligned to risk appetite.</td>
<td></td>
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<tr>
<td>– Enterprise risk management arrangements are embedded in the routine business decision-making process.</td>
<td></td>
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<tr>
<td>– Formal programmes in place to measure/assess the economic, social and environmental impacts of (1) potential acquisitions, (2) technologies to be extended to Emerging Markets, (3) innovative business models, (4) cost-of-quality reduction initiatives, and (5) manufacturing siting, functional optimisation and site utilisation alternatives.</td>
<td></td>
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</tbody>
</table>
Our plan focuses on both the foundational and competitive advantage elements required to deliver our value proposition sustainably. We employ a continuous improvement approach based upon the implementation of forward-looking solutions (such as investing in new materials and processes that provide significant benefits with respect to human rights, safety, energy, waste and/or communities) and bridging technologies to secure future game-changing performance.

**EMPLOYEE SAFETY, WELLNESS AND VOLUNTEERING**
A healthy and safe working environment is fundamental to the way we work at Smith & Nephew. We must ensure that the safety of our employees and those who work with us is given the highest priority when we perform our daily activities in our offices around the world, when we visit customers and in our manufacturing environment.

**SOCIAL RESPONSIBILITY STRATEGY IMPLEMENTATION**
We further improved our understanding of performance against relevant labour standards in both our operations and in our supply chain. We undertook measures to improve performance across the entire business, taking significant steps toward the implementation of the Social Responsibility Strategy which was adopted in 2017.

Our Social Responsibility Strategy aims to improve the alignment of our charitable donations, volunteering, wellness and professional development with both our Group Business Strategy and the needs and desires of our employees. Our goal is to impact positively both employee engagement and the quality of life in communities in which we operate.

In 2018, we improved our understanding of product and service attributes which are important to customers and our employees’ view of the role of the organisation in society.

In 2019, we will further drive labour practice improvements in our supply chain and turn our attention more fully to identifying and delivering the socially responsible attributes which help drive quality of life in the communities in which we operate.

**CO₂e REPORTING METHODOLOGY, MATERIALITY AND SCOPE**
We report the carbon footprint of our Scope 1 and 2 greenhouse gas (GHG) emissions in tonnes of CO₂ equivalent from our business operations for the calendar year ended 31 December 2018. Our focus is on the areas of largest environmental impact including manufacturing sites, warehouses, R&D sites and offices. Smaller locations representing less than 2% of our overall emissions are not included. Acquisitions completed before 2018 are included in the data.

Our GHG emissions reporting represents our core business operations and facilities which fall within the scope of our consolidated financial statements. Primary data from energy suppliers has been used wherever possible.

<table>
<thead>
<tr>
<th></th>
<th>2018</th>
<th>2017</th>
<th>2016</th>
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</thead>
<tbody>
<tr>
<td>CO₂e emissions (tonnes) from:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Direct emissions</td>
<td>9,956</td>
<td>9,451</td>
<td>9,822</td>
</tr>
<tr>
<td>Indirect emissions</td>
<td>67,886</td>
<td>76,107</td>
<td>82,415</td>
</tr>
<tr>
<td>Total</td>
<td>77,842</td>
<td>85,558</td>
<td>92,237</td>
</tr>
<tr>
<td>Intensity ratio</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>CO₂e (t) per $m sales revenue</td>
<td>15.9</td>
<td>17.8</td>
<td>19.6</td>
</tr>
<tr>
<td>CO₂e (t) per full-time employee</td>
<td>4.7</td>
<td>5.2</td>
<td>5.9</td>
</tr>
</tbody>
</table>


We report our emissions in two ‘scopes’.
Scope 1 figures include: Direct sources of emissions which mainly comprise the fuels we use on-site, such as gas and heating oil and fugitive emissions arising mainly from the losses of refrigerant gases.
Scope 2 figures include: Indirect sources of emissions such as purchased electricity and steam we use at our sites.

Location-based emissions are calculated in compliance with the WRI/WBCSD GHG Protocol Corporate Accounting and Reporting Standard and have been calculated using carbon conversion factors published by BEIS/DEFRA for 2018. We have applied the emission factors most relevant to the source data, including DEFRA 2018 (for UK locations), IEA 2016 (for overseas locations) and for the US we have used the most recently available US EPA ‘Emissions & Generation Resource Integrated Database’ (eGRID) for the regions in which we operate. All other emission factors for gas, oil, steam and fugitive emissions are taken from DEFRA 2018.
Our performance

We improved performance, delivered meaningful efficiency savings, and generated good cash flow
Chief Financial Officer’s review

Our performance accelerated across the year and we take good momentum into 2019

DEAR SHAREHOLDER

Smith & Nephew delivered a solid financial performance in 2018. We improved performance, delivered meaningful efficiency savings, sustained investments in R&D for growth and continued to generate strong cash flow. This was achieved while also making important changes to our leadership, structures and culture which all position us well for further progress in 2019 and beyond.

2018 PERFORMANCE

Group revenue in 2018 was $4,904 million, an increase of 3% on a reported basis and 2% on an underlying basis. Our performance accelerated across the year, with 3% revenue growth on an underlying basis in the second half, and we take good momentum into 2019.

The reported operating profit for 2018 was $863 million, an 8% reduction from the previous year primarily reflecting the costs of the Accelerating Performance and Execution (APEX) restructuring programme as described below.

Trading profit for the year was $1,123 million and the trading profit margin was up 90bps to 22.9%. This reflects both the 50bps benefit of a one-off legal settlement and improved trading performance and cost control.

The reported tax rate was 15.1% (2017: 12.7%). The tax rate on trading results for the year to 31 December 2018 was 16.1% (2017: 17.1%). This was lower than the guided rate of between 20–21% mainly due to a one-off benefit from a tax provision release following expiry of statute of limitations and a beneficial geographical mix of profits.

The reported tax rate was lower than the tax rate on trading results as a higher proportion of non-trading items were in higher tax jurisdictions, notably the US.

Basic earnings per share (‘EPS’) was down 13% to 76.0¢, also primarily due to APEX restructuring charges. Adjusted earnings per share (‘EPSA’) was up 7% at 100.9¢, reflecting the legal settlement gain, improved trading performance and the lower tax rate on trading results.

I’m pleased to report that trading cash flow was $951 million, up from $940 million in 2017, and we had another year of strong cash conversion (as defined on page 195) at 85% (2017: 90%). Return On Invested Capital (ROIC) – as defined on page 198 – was 12.5% (2017: 14.3%), reflecting the reduction in operating profit over the prior year noted above.

CAPITAL RETURNS

The appropriate use of capital on behalf of shareholders is important to Smith & Nephew. The Board believes in maintaining an efficient, but prudent, capital structure, while retaining the flexibility to make value enhancing acquisitions. This approach is set out in our Capital Allocation Framework which we used to prioritise the use of cash and ensure an appropriate capital structure.

Our commitment, in order of priority, is to:
1. Continue to invest in the business to drive organic growth;
2. Maintain our progressive dividend policy;
3. Realise acquisitions in-line with strategy, and
4. Return any excess capital to shareholders.

Net debt was $1,104 million at year-end, a decrease of $177 million from $1,281 million at 31 December 2017. As part of our strategy to expand in higher growth markets, we expect to participate actively in value-enhancing M&A opportunities, and I am pleased with progress of our REGENETEN business, acquired from Rotation Medical in Q4 2017, which exceeded expectations throughout 2018. We have a strong balance sheet and substantial capacity for acquisitions. Appropriate financing for larger acquisitions would be considered on a case-by-case basis, as opportunities arise.

CETERIX ACQUISITION

In January 2019 we completed the acquisition of Ceterix Orthopaedics, Inc., the developer of the NovoStitch Pro Meniscal Repair System. The acquisition supports the Company’s strategy to invest in innovative technologies that address unmet clinical needs. The cost of the acquisition was $45 million upon completion, $5 million deferred and up to a further $55 million over the next five years, contingent on financial performance.

EFFICIENCY

Our new Strategic Imperatives include Become the Best Owner. One of the ways we will do this is through simplifying the organisation and its processes, including through the APEX programme, initiated at the end of 2017.

We are on track across all three workstreams of 1) Manufacturing, Warehousing and Distribution, 2) General and Administrative (G&A) Expenses, and 3) Commercial Effectiveness. APEX is expected to drive an annualised benefit of $160 million by 2022 for a one-off cost of $240 million.
In 2018, APEX incurred restructuring costs of $120 million with actions undertaken that resulted in benefits of approximately $60 million in the year.

Graham Baker
Chief Financial Officer

We continue to keep the programme under review to ensure the delivery of benefits and assess any further incremental opportunities that may arise.

In 2018, APEX incurred restructuring costs of $120 million with actions undertaken that resulted in benefits of approximately $60 million in the year.

During the year, I was pleased to take on responsibility for our Global Business Services (GBS) and IT functions. Both functions have important roles to play both in supporting delivery of the business strategy and delivering efficiencies as part of the APEX programme.

Expert people, improved systems and effective processes are core to those functions and both functions provide high quality service to the business from a mixture of locations, both near to our business and in cost effective regional centres.

We now have fully functioning GBS centres in Costa Rica, Malaysia, India and Poland. Our employees in these locations are integral members of the Smith & Nephew team and we expect all the centres to expand to take on more work in the coming year.

UK’S WITHDRAWAL FROM THE EU

The Group does not believe that the UK’s decision to leave the EU will have a significant impact on our long-term ability to conduct business into and out of the EU or UK. We are making good progress with our preparations for the various scenarios. Early in 2019, our preparations were assessed by external advisors on behalf of the Internal Audit function, with the findings reviewed by the Audit Committee.

OUTLOOK

Our 2019 guidance for further improvement in underlying performance at the top and bottom line is an important step in realising our medium-term ambition to outgrow our markets.

In terms of revenue, we expect our underlying growth to be in the range of 2.5% to 3.5% in 2019. On a reported basis this equates to a range of around 1.8% to 2.8% at exchange rates prevailing on 1 February 2019 and including the effect of the Ceterix acquisition.

We expect 2019 trading profit margin to be in the range of 22.8% to 23.2%, a further 40–80bps improvement over 2018, excluding the one-off 50bps legal settlement benefit.

The tax rate on trading results for 2019 is expected to be in the range 19% to 21%, subject to any material changes to tax law, or other one-off items.

Following the implementation of the new franchise-based organisational structure from January 2019, we have concluded that we will have reportable segments for our three main franchises, Orthopaedics, Sports Medicine & ENT and Advanced Wound Management, from 2019 onwards. I hope that investors and others will benefit from the additional information this will provide.

Yours sincerely,

Graham Baker
Chief Financial Officer

REVENUE

$4,904m

<table>
<thead>
<tr>
<th>REPORTED</th>
<th>UNDERLYING¹</th>
</tr>
</thead>
<tbody>
<tr>
<td>+3%</td>
<td>+2%</td>
</tr>
</tbody>
</table>

EARNINGS PER SHARE

76.0c

-13%

ADJUSTED EARNINGS PER SHARE² (EPSA)

100.9c

+7%

¹ These non-IFRS financial measures are explained and reconciled to the most directly comparable financial measure prepared in accordance with IFRS on pages 194–195.

² Net debt is reconciled in Note 15 to the Group accounts.
Financial review

We have a strong balance sheet and substantial capacity for acquisitions

**GROUP PERFORMANCE**

<table>
<thead>
<tr>
<th></th>
<th>2018 $ million</th>
<th>2017 $ million</th>
<th>Change $ million</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Consolidated income statement</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Revenue</td>
<td>4,904</td>
<td>4,765</td>
<td>139</td>
</tr>
<tr>
<td>Operating profit</td>
<td>863</td>
<td>934</td>
<td>(71)</td>
</tr>
<tr>
<td>Trading profit</td>
<td>1,123</td>
<td>1,048</td>
<td>75</td>
</tr>
<tr>
<td>Profit before tax</td>
<td>761</td>
<td>879</td>
<td>(98)</td>
</tr>
<tr>
<td>Attributable profit</td>
<td>663</td>
<td>767</td>
<td>(104)</td>
</tr>
<tr>
<td>EPS</td>
<td>76.0e</td>
<td>87.8e</td>
<td>(11.8e)</td>
</tr>
<tr>
<td>EPISA</td>
<td>100.9e</td>
<td>94.5e</td>
<td>6.4e</td>
</tr>
</tbody>
</table>

**NON-IFRS MEASURES**

The underlying increase in revenues by market reconciles to reported growth, the most directly comparable financial measure calculated in accordance with International Financial Reporting Standards (IFRS), as follows:

<table>
<thead>
<tr>
<th></th>
<th>2018 $ million</th>
<th>2017 $ million</th>
<th>Reported growth %</th>
<th>Underlying growth %</th>
<th>Acquisitions/Disposals %</th>
<th>Currency impact %</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>US</strong></td>
<td>2,354</td>
<td>2,306</td>
<td>2%</td>
<td>1%</td>
<td>1%</td>
<td>0%</td>
</tr>
<tr>
<td>Other Established Markets</td>
<td>1,693</td>
<td>1,658</td>
<td>2%</td>
<td>0%</td>
<td>0%</td>
<td>2%</td>
</tr>
<tr>
<td>Emerging Markets</td>
<td>857</td>
<td>801</td>
<td>7%</td>
<td>8%</td>
<td>0%</td>
<td>(1%)</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>4,904</td>
<td>4,765</td>
<td>3%</td>
<td>2%</td>
<td>0%</td>
<td>1%</td>
</tr>
</tbody>
</table>

Trading profit reconciles to operating profit, the most directly comparable financial measure calculated in accordance with IFRS, as follows:

<table>
<thead>
<tr>
<th></th>
<th>2018 $ million</th>
<th>2018 %</th>
<th>2017 $ million</th>
<th>2017 %</th>
<th>2017 %</th>
<th>2017 %</th>
</tr>
</thead>
<tbody>
<tr>
<td>Operating profit</td>
<td>863</td>
<td>17.6%</td>
<td>934</td>
<td>19.6%</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Acquisition and disposal related items</td>
<td>(7)</td>
<td>(0.1%)</td>
<td>(10)</td>
<td>(0.2%)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Restructuring and rationalisation costs</td>
<td>120</td>
<td>2.4%</td>
<td>–</td>
<td>–</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Amortisation and impairment of acquisition intangibles</td>
<td>113</td>
<td>2.3%</td>
<td>140</td>
<td>2.9%</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Legal and other</td>
<td>34</td>
<td>0.7%</td>
<td>(16)</td>
<td>(0.3%)</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Trading profit</strong></td>
<td>1,123</td>
<td>22.9%</td>
<td>1,048</td>
<td>22.0%</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

**DIVIDENDS**

The 2017 final dividend of 22.7 US cents per ordinary share totalling $198 million was paid on 9 May 2018. The 2018 interim dividend of 14.0 US cents per ordinary share totalling $123 million was paid on 31 October 2018.

**RETURN ON INVESTED CAPITAL**

Return On Invested Capital (ROIC) is a measure of the return generated on capital invested by the Group. It provides a metric for long-term value creation and encourages compounding reinvestment within the business and discipline around acquisitions with low returns and long payback. ROIC decreased from 14.3% in 2017 to 12.5% in 2018 as a result of the reduction in operating profit.

ROIC is defined as:

\[
\text{Net Operating Profit less Adjusted Taxes} / (\text{Opening Net Operating Assets} + \text{Closing Net Operating Assets})/2
\]
BALANCE SHEET

<table>
<thead>
<tr>
<th></th>
<th>2018</th>
<th>2017</th>
<th>Change</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>$ million</td>
<td>$ million</td>
<td>$ million</td>
</tr>
<tr>
<td><strong>Consolidated balance sheet</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Goodwill and intangible assets</td>
<td>3,547</td>
<td>3,742</td>
<td>(195)</td>
</tr>
<tr>
<td>Other non-current assets</td>
<td>1,435</td>
<td>1,393</td>
<td>42</td>
</tr>
<tr>
<td>Current assets</td>
<td>3,077</td>
<td>2,731</td>
<td>346</td>
</tr>
<tr>
<td>Total assets</td>
<td>8,059</td>
<td>7,866</td>
<td>193</td>
</tr>
<tr>
<td>Total equity</td>
<td>4,874</td>
<td>4,644</td>
<td>230</td>
</tr>
<tr>
<td>Non-current liabilities</td>
<td>1,720</td>
<td>1,876</td>
<td>(156)</td>
</tr>
<tr>
<td>Current liabilities</td>
<td>1,465</td>
<td>1,346</td>
<td>119</td>
</tr>
<tr>
<td>Total liabilities</td>
<td>3,185</td>
<td>3,222</td>
<td>(37)</td>
</tr>
<tr>
<td>Total liabilities and equity</td>
<td>8,059</td>
<td>7,866</td>
<td>193</td>
</tr>
<tr>
<td>Net debt1</td>
<td>1,104</td>
<td>1,281</td>
<td>(177)</td>
</tr>
</tbody>
</table>

Goodwill decreased by $34 million primarily as a result of foreign currency movements. Intangible assets decreased by $161 million with amortisation and impairment of $79 million and foreign currency movements of $14 million partially offset by net additions of $32 million.

Other non-current assets increased by $42 million primarily due to an increase of $30 million in the retirement benefit assets for our UK and US pension schemes. Trade investments also increased by $13 million as a result of additions of $4 million and fair value re-measurements of $9 million. Current assets increased by $346 million with trade and other receivables increasing $59 million as a result of the timing of collections, inventories increasing $91 million primarily due to sales growth and new product build, and cash increasing $196 million due to insurance recoveries and stronger underlying profits.

Non-current liabilities decreased by $156 million primarily due to the reclassification of certain payables and borrowings to current liabilities, as they now fall due within one year. Current liabilities increased by $119 million as a result of the aforementioned reclassifications from non-current to current liabilities and an increase of $18 million in bank overdrafts.

LIQUIDITY AND CAPITAL RESOURCES

The Group’s policy is to ensure that it has sufficient funding and facilities in place to meet foreseeable borrowing requirements.

The Group’s net debt1 decreased from $1,281 million at the beginning of 2018 to $1,104 million at the end of 2018, representing an overall decrease of $177 million.

At 31 December 2018, the Group held $333 million (2017: $155 million) in cash net of bank overdrafts. The Group had committed facilities available of $2,429 million at 31 December 2018 of which $1,429 million was drawn. Smith & Nephew intends to repay the $125 million of facilities due within one year by using available cash and drawing down on the longer-term facilities.

The principal variations in the Group’s borrowing requirements result from the timing of dividend payments, acquisitions and disposals of businesses, timing of capital expenditure and working capital fluctuations. Smith & Nephew believes that its capital expenditure needs and its working capital funding for 2019, as well as its other known or expected commitments or liabilities, can be met from its existing resources and facilities.

The Group’s planned future contributions are considered adequate to cover the current underfunded position in the Group’s defined benefit plans.

CASH FLOW STATEMENT

<table>
<thead>
<tr>
<th></th>
<th>2018</th>
<th>2017</th>
<th>Change</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>$ million</td>
<td>$ million</td>
<td>$ million</td>
</tr>
<tr>
<td><strong>Consolidated cash flow statement</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cash generated from operations</td>
<td>1,108</td>
<td>1,273</td>
<td>(165)</td>
</tr>
<tr>
<td>Trading cash flow1</td>
<td>951</td>
<td>940</td>
<td>11</td>
</tr>
<tr>
<td>Free cash flow1</td>
<td>584</td>
<td>714</td>
<td>(130)</td>
</tr>
</tbody>
</table>

Cash generated from operations of $1,108 million is after paying out $3 million of acquisition and disposal related items, $83 million of restructuring and rationalisation expenses and $104 million relating to legal and other costs.

Trading cash flow increased by $11 million driven by higher trading profit and lower capital expenditure. These movements were partly offset by a working capital net outflow which included an increase in inventory as described above. Free cash flow1 decreased by $130 million primarily related to higher cash outflows for restructuring and rationalisation expenses and legal and other costs.

During the year ended 31 December 2018, the Group purchased a total of 2.7 million (2017: 3.2 million) ordinary shares at a cost of $48 million (2017: $52 million) as part of the ongoing programme to buy back an equivalent number of shares to those vesting as part of the employee share plans.

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1 These non-IFRS financial measures are explained and reconciled to the most directly comparable financial measure prepared in accordance with IFRS on pages 194–198.

2 Included within the 2017 analysis is a reclassification of $20 million of revenue formerly included in Other Established Markets which has now been included in Emerging Markets in order to present consistent analysis to the 2018 results.

3 Net debt is reconciled in Note 15 to the Group accounts.
Risk report

Our risk management process

Our approach to risk

Like all businesses, we face a number of risks and uncertainties.

Some come from outside our organisation, others from within. Some we can’t control, some we can. Many of our risks are similar to those experienced by similar businesses and for 2018 we are undoubtedly aligned with other businesses as risks around Brexit uncertainty and political unrest globally have heightened.

Successful management of existing and emerging risks is critical to the long-term success of our business and to the achievement of our strategic objectives. In order to seize market opportunities and leverage the potential for success, risk must be accepted to a reasonable degree within our tolerances. Risk management is therefore an integral component of the Group’s Corporate Governance.

As in previous years our Enterprise Risk Management process is based on a holistic approach to risk management, leveraging risk identification and risk treatments already in place throughout our Business Areas whilst incorporating the same risk processes into the strategic planning process. Our belief is that the strategic and operational benefits of managing risk are achieved when Enterprise Risk Management is aligned with the strategic and operational goals of the organisation, and our process and governance structure firmly aligns to this approach.

The current financial year has seen further maturity of the risk management framework with further testing of key controls through ‘deep dives’ by the Group Risk Team and a number of different risk topics presented to the Board and its Committees. We have also designed our Enterprise Risk Management Framework to be fully integrated into our business processes. This will be built on further throughout 2019.

Our risk governance framework is set out below. At the very top of our structure is our Board, setting our risk appetite and monitoring the application of our risk framework through strategy, execution and practically through the outputs of regular risk ‘deep dives’ and reviews by the business and Group Risk Team. The Board cascades our risk appetite throughout our organisation through the Executive Committee, risk owner community and our management group with a formal ‘bottom up’ process ensuring that risks are escalated back through the process to our Board and form our Principal Risks as appropriate. Providing rigour and independence across this process is our Executive Committee and the Group Risk Team.

At the third line of defence is our Internal Audit Function, providing an annual opinion on the effectiveness of our Risk Management process to the Executive Committee, chaired by the Chief Executive Officer, and then to the Board and its Committees.

**BOARD OF DIRECTORS AND BOARD COMMITTEES**
- Responsible for regular oversight of risk management and for our annual strategic risk review
- Monitors risks through Board processes (Strategy Review, Disclosures, M&A, Investments, Disposals) and Committees (Audit and Compliance & Culture), management reviews and ‘deep dives’ of selected risk areas
- The Audit Committee is responsible for ensuring oversight of the process by which risks relating to the Company and its operations are managed and for reviewing the operating effectiveness of the Group’s Risk Management process
**EXECUTIVE COMMITTEE SITTING AS GROUP RISK COMMITTEE**

- Reviews external/internal environment for emerging risks
- Reviews risk register updates from Business Area Risk Groups
- Identifies significant risks and assesses effectiveness of mitigating actions

**BUSINESS AREA**

- Business Area Risk Champions provide support to ensure a framework is designed and implemented for alignment to the requirements of the Enterprise Risk Management Framework
- Carry out day-to-day risk management activities
- Identify and assess risk
- Implement strategy and mitigating actions to treat risk within Business Area
- Business Area Risk Champions lead regular risk register updates

**GROUP RISK TEAM**

- Manages implementation of all aspects of the Group’s approach to Enterprise Risk Management including implementation of processes, tools and systems to identify, assess, measure, manage, monitor and report risks
- Facilitates implementation and coordination through Business Area Risk Champions
- Provides resources and training to support process
- Regular risk reporting to the Executive Committee
- Prepares Board and Group Risk Committee reports

**ANNUAL ASSESSMENT OF EFFECTIVENESS – INTERNAL AUDIT AND CONTROL FUNCTIONS**

- Provides independent assurance to the Board and Audit Committee on the effectiveness of the Group’s Risk Management process

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**Risk management life cycle**

Our risk management life cycle was fully refreshed in 2017 and was updated in 2018 to align with our new strategic imperatives which we launched in December.

Our Risk Management Policy, sponsored by our Chief Executive Officer, is supported by an Enterprise Risk Management Manual and the risk team provide regular training to all risk champions throughout the year. As in 2018 risks continue to be managed through a ‘bottom up’ and ‘top down’ process, with regular oversight from the Executive Committee and quarterly reports to the Board Committees. An overview of our risk management life cycle can be found below:

1. **Risk identification**
   - **IDENTIFYING** risks associated with the achievement of our objectives by function at the Group level.

2. **Gross (inherent) risk assessment**
   - **ASSESSING** the level of inherent (gross) risk.

3. **Current control identification**
   - **IDENTIFYING** existing controls to mitigate risks.

4. **Net (residual) risk**
   - **ASSESSING** the level of residual (net) risk after mitigation so that risk levels are managed within defined tolerance thresholds without being over-controlled or foregoing desirable opportunities.

5. **Risk response planning**
   - **IDENTIFYING** additional actions required to meet our expected risk tolerance level and **ASSIGNING** risk owners, timeframes and actions for ongoing management and reporting.

6. **Risk reporting**
   - **REPORTING** the status of our most significant risks through the ‘bottom up’ business area processes and the ‘top down’ Executive Committee and Board process.

7. **Monitoring and review**
   - **MONITORING** of risks and actions by management, the accountable Executive and Board.
2018 principal risks

We assess our Principal Risks in terms of their potential impact on our ability to deliver our Strategic Imperatives

These links are highlighted across the following pages and further information on the Strategic Imperatives is found on page 9.

BUSINESS CONTINUITY AND BUSINESS CHANGE

Operating with a global remit, increased outsourcing, more sophisticated materials and the speed of technological change in an already complex manufacturing process leads to greater potential for disruptive events. Ensuring our ability to continually execute and operate key sites and facilities in order to develop, manufacture and sell our products within this environment is a key strategic imperative of the organisation.

In addition, the pace and scope of our business ‘change’ initiatives increases the execution risk that benefits may not be fully realised, costs of these changes may increase, or that our business as usual activities may not perform in-line with our plans.

Examples of risks

- Failure or significant performance issues experienced at critical/single source facilities.
- Disruption to manufacturing at single or sole source facility (lack of manufacturing redundancy).
- Supplier failure impacts ability to meet customer demand (single source suppliers).
- Natural disaster impacts ability to meet customer demand.
- Significant ‘change’ prevents our projects and programmes such as APEX achieving the intended benefits and disrupts existing business activities.

Risk Tolerance

In operating our business, executing our change programmes and in managing our suppliers and facilities we have a low to moderate tolerance for this risk.

Change from 2017

No change.

Actions taken by management

- Comprehensive product quality processes and controls are in place from design to customer supply.
- Emergency and incident management and business recovery plans are in place at major facilities and for key products and key suppliers.
- Undertaking risk based review programmes for critical suppliers.
- Project management governance and toolkits and project steering committee oversight to support successful execution of programme and projects.
- Executive Committee and Audit Committee oversight of Risks to change programmes.
- Brexit Steering Group regularly monitors the evolving impact of Brexit and oversees our response.

Link to strategy

Our Strategic Imperative to ‘Become the best owner’ requires us to ensure we remain sustainable into the future and through periods of business change.

Oversight

Board
CYBER SECURITY

High profile incidents coupled with increasing government focus has resulted in raised awareness of the extent and potential impact of cyber security breaches. Our increasing business dependence on networked systems and the internet, the design of new products, connectable products and embedded software and the rapidly evolving cyber security threat landscape provides a level of risk exposure not experienced in prior years. In response to this we have undertaken an exercise to understand our threats and vulnerabilities to target cyber security investment in the right places.

Examples of risks
- Loss of intellectual property/major data privacy breach or significant impact on business operations from Malware or Ransomware outbreak.
- Cyber security is not considered in the design of new products with more products being connectable/having embedded software.

Risk Tolerance
In managing our cyber risk and the possible disruption and reputational impact we have a low to moderate tolerance for Cyber Security Risk.

Change from 2017
No change.

Actions taken by management
- Security information and event management (SIEM) in place provides real-time analysis of security alerts generated by applications and network hardware.
- Annual penetration testing and quarterly vulnerability testing. Endpoint protection and Intrusion detection/prevention.
- The adoption of additional authentication tools to reduce the likelihood of remote attacks.
- Annual mandatory training and continuous awareness training for end-users.
- Security governance structure in place including a Cyber Security Steering Committee.
- Further strengthening governance including a programme to monitor cyber security capabilities and controls, technical and governance matters.

Link to strategy
Our Strategic Imperative to ‘Transform the business through enabling technologies’ requires us to deliver technology solutions in compliance with laws and regulations and in a way that protects any vulnerability to Cyber Risk.

QUALITY AND REGULATORY

Global regulatory bodies continue to increase their expectations of manufacturers and distributors of medical devices. Our products are used in the human body and therefore patient safety is of paramount importance. The European Medical Device Regulations, launch of ISO13485:2016, the Medical Device Single Audit Programme and the tightening of the Chinese YY standards have increased the focus on clinical and technical evidence, supplier controls and continual product risk reduction.

2018 has also brought uncertainty in terms of Britain’s exit from the EU as well as future trade and regulatory relations between the EU and UK. Like many other companies we are planning for the impact of a range of eventualities, particularly in continuity assessment and how our products will continue to be appropriately registered for trade around the EU.

Examples of risks
- Defects in design or manufacturing of products supplied to, and sold by, the Group could lead to product recalls or product removal or result in loss of life or major injury.
- Significant non-compliance with policy, regulations or standards governing products and operations regarding registration, manufacturing, distribution, sales or marketing.
- Failure to obtain proper approvals for new or changed technologies, products or processes.
- CE certificates issued by UK notified bodies prior to the withdrawal date may be rendered void post Brexit.

Risk Tolerance
Our response to this risk continues to be critical and our ability to align the standards required to ensure safe and compliant products is the key driver for our extremely low tolerance for risk in this area.

Change from 2017
No change.

Actions taken by management
- Comprehensive and documented product quality processes and controls from design to customer distribution are in place.
- Standardised monitoring and compliance with quality management practices through our Global Quality Assurance and Regulatory Affairs organisation.
- Incident management teams in place to respond immediately in the event of an incident relating to patient safety.
- Governance framework in place for reporting, investigating and responding to instances of product safety and complaints.
- Brexit working group is in place considering various deal/no deal scenarios.

Link to strategy
Our Strategic Imperative to ‘Become the best owner’ requires us to operate effectively and efficiently and to produce compliant products of the highest quality to provide safe and effective solutions to our customers.

Oversight
Board Compliance & Culture Committee.
### NEW PRODUCT INNOVATION, DESIGN & DEVELOPMENT INCLUDING INTELLECTUAL PROPERTY

Our product portfolio is becoming increasingly complex, especially as we move to more innovative connected product technologies. Our success relies on investing in safe products and platforms, aligned internal and external design, and development innovation in order to compete effectively. The need to be considered in our approach to protecting our products, process and intellectual property is essential.

#### Examples of risks
- Failure to develop an appropriate pipeline of commercially successful products to meet and anticipate the needs of our customers ahead of the competition.
- Insufficient long-term planning to respond to competitor disruptive entries into marketspace.
- Inadequate innovation due to low Research & Development (R&D) investment, R&D skills gap or poor product development execution.
- Lower value business segment investment, such as product maintenance and line extension projects.
- Competitors may assert patents or other intellectual property rights against the Company, or fail to respect the Company’s intellectual property rights.

#### Actions taken by management
- Global R&D organisation and governance framework providing strategic direction for allocation of R&D investments across all businesses. Clear stage-gate process to continually evaluate R&D investments decisions and development of new products.
- Enhanced relationship with Commercial team to focus on developing products that customers need.
- Strengthened Clinical Affairs programme integrated with Global Marketing.
- Cross functional New Product Design and R&D processes focused on identifying new products and potentially disruptive technologies and solutions.
- Monitoring of external market trends and collation of customer insights to develop product strategies.
- Careful attention to intellectual property considerations.

#### Risk Tolerance
In pursuit of our strategy to be innovative in our product offering we have a moderate to high tolerance for risk.

#### Change from 2017
Reduced risk.

#### Link to strategy
Our Strategic Imperative to ‘Transform the business through enabling technologies’ depends heavily on our ability to continue to develop new innovative products and bring them to market.

#### Oversight
Board

### TALENT MANAGEMENT

We recognise that people management, effective succession planning and the ability to attract and retain talent is of great importance to the success of our Company. In the current economic environment of strong competition and reduced spending, retention of top talent is a critical risk which requires a strong process in relation to retention and engagement. Failure to do so can result in risks in our ability to execute Company strategy and achieve business objectives in relevant functions and to be effective in the chosen market/discipline and leadership of newer workforce which may impact the Company’s future success.

#### Examples of risks
- Loss of key talent, high attrition and lack of appropriate succession planning in context of required skillsets for future business needs.
- Loss of competitive advantage due to an inability to attract and retain Top Talent.
- Loss of intellectual capital due to poor retention of talent.

#### Actions taken by management
- Talent planning and people development processes are well established across the Group. Talent and succession planning is discussed annually by the Board and regularly by the Executive Committee and Nomination & Governance Committee.
- Identification of high performing individuals and practices to plan for the succession of key roles.
- Consistent and robust performance management process.
- Development of strategic skills resourcing plan by functional areas.

#### Risk Tolerance
We have a moderate tolerance for this risk.

#### Change from 2017
No change.

#### Link to strategy
All our strategic imperatives rely on ensuring we have the right talent within our organisation to deliver maximum efficiency in everything we do and to build strong leaders for the future.

#### Oversight
Board
## PRICING AND REIMBURSEMENT

Our success depends on our ability to sell our products profitably in spite of increasing pricing pressures from customers, and governments providing adequate funding to meet increasing demands arising from demographic trends. The prices we charge are therefore impacted by budgetary constraints and our ability to persuade customers and governments of the economic value of our products, based on clinical data, cost, patient outcomes and comparative effectiveness.

We further face challenging market dynamics, such as consolidation of customers into buying groups, increasing professionalisation of procurement departments and the commoditisation of entire product groups, which continue to challenge prices.

### Examples of risks
- Reduced reimbursement levels and increasing pricing pressures.
- Systemic challenge on number of elective procedures.
- Lack of compelling health economics data to support reimbursement requests.
- Risk of adverse trading margins due to fluctuating foreign currency exchange rates across our main manufacturing countries (US, UK, Costa Rica and China) and where our products are sold.

### Risk Tolerance
In implementing innovative pricing strategies, we have a moderate to high tolerance for risk and are willing to accept certain risks in pursuit of new business opportunities.

### Change from 2017
No change.

### Actions taken by management
- Development of innovative economic product and service solutions for both Established and Emerging Markets.
- Appropriate breadth of portfolio and geographic spread to mitigate exposure to localised risks.
- Incorporating health economic components into the design and development of new products.
- Emphasising value propositions tailored to specific stakeholders and geographies through strategic investment and marketing programmes.

### Link to strategy
Our Strategic Imperative to ‘Achieve the full potential of our portfolio’ depends on our ability to sell our products profitably in spite of increased pricing pressures from payers.

### Oversight
Board

## MERGERS AND ACQUISITIONS

As the Company grows to meet the needs of our customers and patients, we recognise that we are not able to develop all the products and services required using internal resources and therefore need to undertake mergers and acquisitions in order to expand our offering and to complement our existing business. In other areas, we may divest businesses which are no longer core to our activities. It is crucial for our long-term success that we make the right choices around acquisitions and divestments.

We have a well-defined cross-functional process for managing risks associated with mergers and acquisitions that is subject to scrutiny from executive management and the Board of Directors.

### Examples of risks
- Failure to identify appropriate acquisitions or to conduct effective acquisition due diligence.
- Failure to integrate newly acquired businesses effectively, including integration with Company standards, policies and financial controls.

### Risk Tolerance
In acquiring new businesses and business models, we have a moderate to high tolerance for commercial risk and are willing to accept certain risks in pursuit of new business.

### Change from 2017
No change.

### Actions taken by management
- Acquisition activity is aligned with corporate strategy and prioritised towards products, franchises and markets identified to have the greatest long-term potential.
- Clearly defined investment appraisal process based on return on capital, in accordance with Capital Allocation Framework and comprehensive post-acquisition review programme.
- Undertaking detailed and comprehensive cross-functional due diligence prior to acquisitions.
- Compliance risks included as part of due diligence reviews, integration plans and reporting for acquisitions.

### Link to strategy
Our Strategic Imperatives to ‘Expand in high-growth segments’ and ‘Transform the business through enabling technologies’ depend on our ability to identify the right acquisitions, to conduct thorough due diligence and to integrate acquisitions effectively.

### Oversight
Board
### LEGAL AND COMPLIANCE RISKS

Our global remit results in heavy regulation across multiple jurisdictions. There is increasing public scrutiny of ethics in business and ‘doing the right thing’ is part of our licence to operate. National regulatory authorities enforce a complex pattern of laws and regulations that govern the design, development, approval, manufacture, labelling, marketing and sale of healthcare products.

Operating across this increasingly complex and dynamic legal and compliance environment, including regulations on bribery and corruption, with poor legal and compliance practices can lead to fines, penalties, reputational risk and competitive disadvantage. We have adopted a proactive, holistic approach, which guides the Company towards a culture of compliance and turns the resolution of legal and compliance issues into a source of competitive advantage.

#### Examples of risks
- Failure to act in an ethical manner consistent with our Code of Conduct.
- Violation of anti-corruption or healthcare laws, breach by employee or third party representative.
- Misuse or loss of personal information of patients, employees, research subjects, consumers or customers results in violations of data privacy laws, including General Data Protection Regulations.

#### Risk Tolerance
In complying with legal and compliance requirements, we have an extremely low tolerance.

#### Change from 2017
No change.

#### Actions taken by management
- Ethics & Compliance Committee oversees our ethical and compliance practices.
- Global compliance programme, policies and procedures.
- All employees are required to undertake annual training and to certify compliance on an annual basis with our Code of Conduct and Business Principles.
- Group monitoring and auditing programmes in place.
- Confidential independent reporting channels for employees and third parties to report concerns.

#### Link to strategy
Our Strategic Imperative to ‘Become the best owner’ requires us to comply with applicable laws and regulations and do the right thing as part of our licence to operate.

#### Oversight
Board Compliance & Culture Committee

### COMMERCIAL EXECUTION

We continue to make good and strong progress delivering our priorities and are proud of the pace with which our strategic and operational decisions are quickly translated into actions. Effective communication and engagement with our customers are critical to the long-term success of our business. We are confident that we have the right priorities, structures and capabilities across the Group and we acknowledge that only strong and continued execution will keep us ahead of our competitors and best placed to serve our customers. Failure to execute our priorities will impact our ability to continue to grow our business and serve our customers.

#### Examples of risks
- Failure to execute our strategy adequately from high-level ambition to specific actions to make the ambition a reality.
- Inability to keep pace with significant product innovation and technical advances to develop commercially viable products.
- Failure to adapt our priorities and execution appropriately when conditions change meaning that transformational programmes do not deliver the expected outcomes.
- Failure to engage effectively with our key stakeholders to meet their evolving needs leading to loss of customers.

#### Risk Tolerance
We have a low to moderate tolerance level for commercial execution risk.

#### Change from 2017
No change.

#### Actions taken by management
- Global R&D organisation and supporting governance framework.
- Improved market development and launch execution – commitment to win profitably in our target markets.
- Strategic planning processes clearly linked to business and Group Risk.
- Global transformational programmes in place providing agile opportunities for efficiencies, growth and a strengthened competitive position.

#### Link to strategy
Our Strategic Imperatives to ‘Achieve the full potential of our portfolio’, ‘Transform the business through enabling technologies’ and ‘Expand in high-growth segments’ requires excellent commercial execution.

#### Oversight
Board
Across our business we are exposed to the effects of political and economic risks from the impact of Brexit to changes in the regulatory and competitive landscape to the impact of the US Administration’s changed approach to Trade Policy.

Turning to Brexit, there remain heightened levels of political and regulatory uncertainty in the UK following the referendum vote to leave the EU in June 2016, the triggering of Article 50 in March 2017 and the general election in June 2017. This uncertainty is expected to continue for the foreseeable future until EU exit negotiations have been completed and alternative trade deals have been put in place. This situation may adversely impact trading performance across the sector. Regulatory risk forms the most significant risk presently; the ability for us to continue to manufacture and register our products in a compliant manner for global distribution is key.

Examples of risks
- Macro-economic uncertainty or downturn in the UK economy as a result of Brexit.
- Regulatory risk whereby certificates issued by UK Notified Bodies are no longer recognised in EU following March 2019.
- Global political uncertainty – regarding trade policy.
- Implementation of healthcare reforms and/or protectionist measures and regulation or legislation in local markets.
- Exchange rate volatility.
- The availability of markets and market access rights.
- Impact on strategy and operations.
- Increases in import and labour costs.
- Retention of skilled labour and recruitment concerns.
- Increases in tariffs and restrictions on global trade.

Actions taken by management
- Continued engagement with governments, administrations and regulatory bodies.
- The Group has a Brexit committee which meets regularly and is split into a number different work streams namely:
  - Regulatory – the most complex work stream considering product registration.
  - Supply chain – considering the impacts on import and export requirements in UK and Europe; supply routes, managing inventory levels in the UK and Europe to minimise disruption from border clearance and managing labelling changes required as a result of the regulatory changes.
  - UK and Ireland (‘UKI’) market – considering issues expected to impact the UK specifically the Irish border issue – including whether a changed route to market is required in Ireland.
  - HR – considering issues such as impact on EU workers currently employed in UK and future mobility considerations.
  - Finance – considering issues such as impact on tax including EU trading arrangements and the VAT implications of the changes and the impact on financial reporting, eg EU/UK endorsement of IFRS.
- Improved engagement and monitoring/lobbying on localisation initiatives.

Risk Tolerance
In preparing for Brexit and managing risk arising from changes to our political economical environment, we have a low to moderate tolerance.

Change from 2017
New risk previously incorporated into Business Change.

Link to strategy
Our Strategic Imperative to ‘Become the best owner’ requires us to operate effectively within different global political situations, which change constantly.

Oversight
Board
‘Deep Dives’ and reviews completed in the year

During the year, the risks identified through the ‘bottom up’ and ‘top down’ processes were mapped against each other with the most significant risks forming our Principal Risks.

These risks and our tolerance levels were discussed with each member of the Executive Committee separately and collectively in September and were presented to the Board during the Strategy Review in December 2018. In December, the Accountable Executives were further required to validate that the risk profile had not significantly changed since the initial exercise in June. No changes were required to our risk profile as a result of this exercise, which was also formally validated by each Accountable Executive.

Throughout 2018, the Board assessed and monitored risk in a number of areas and specific ‘Deep Dive’ reviews were also completed by the Group Risk team. In addition, in early 2019, the Board reviewed the results of a deep dive on Brexit risk. The 2018 risk reviews and deep dives included:

<table>
<thead>
<tr>
<th>BOARD AND AUDIT COMMITTEE ‘DEEP DIVES’ AND REVIEWS</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>LEGAL, COMPLIANCE AND QUALITY</strong></td>
</tr>
<tr>
<td>During the year, the Ethics &amp; Compliance Committee considered papers from the quality and regulatory and legal and compliance functions covering topics such as preparations for EU Medical Device Regulations, FDA &amp; Notified Body inspections, outcomes of internal investigations, reviews of legal issues and a review of sexual harassment policies and claims.</td>
</tr>
<tr>
<td><strong>RESEARCH AND DEVELOPMENT</strong></td>
</tr>
<tr>
<td>During the year, the Board received a report from the R&amp;D function which included a focus on the risks associated with the R&amp;D programme and strategies to manage these risks.</td>
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<tr>
<td><strong>FUNCTIONAL OVERSIGHT</strong></td>
</tr>
<tr>
<td>The Board and Audit Committee receive regular updates throughout the year from functions such as IT, Tax, Treasury and Financial Operations. The Audit Committee also receives an update three times a year on the progress of the risk management programme.</td>
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<table>
<thead>
<tr>
<th>MANUFACTURING OPERATIONS</th>
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<tbody>
<tr>
<td>During the year, the Board has received a number of presentations from the global operations team considering the risks in particular associated with the manufacturing footprint and the supply chain and proposals to mitigate these risks.</td>
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<thead>
<tr>
<th>HR</th>
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<tr>
<td>The Board has reviewed and approved all Executive Officer changes during the year within the context of the overall strategy and have been kept updated on management actions to implement the new culture pillars.</td>
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<thead>
<tr>
<th>M&amp;A</th>
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<tbody>
<tr>
<td>Each Board meeting considers Corporate Development within the context of the Group Strategy and also reviews specific acquisitions. During the year, the Board also undertook retrospective reviews of previous acquisitions compared to expectations in the original deal models.</td>
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<thead>
<tr>
<th>IT/CYBER</th>
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<tbody>
<tr>
<td>The Audit Committee received reports on IT and cyber security including an assessment of the existing risks and benchmarking against industry standards.</td>
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<tr>
<th>GROUP RISK TEAM ‘DEEP DIVES’</th>
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<tbody>
<tr>
<td>A series of planned ‘Deep Dives’ have been completed in the year across our Business Risk Areas, including Global Manufacturing, Strategic Sourcing, Supply Chain, Global Quality and Regulatory, Global Business Services and IT. These reviews were introduced in 2017 to supplement reports provided to the Board and primarily cover an ‘independent’ assessment of compliance to the expected Risk Management Framework and in particular the adequacy of stated mitigating activities. The results are reported through the Risk Champions and Accountable Executives to the Audit Committee and are tracked and monitored to resolution by the Group Risk Team.</td>
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</tbody>
</table>
**2019 Risk Management Plan**

Our work will continue to evolve in 2019 and we will strengthen our approach to managing risks across the organisation, including our business areas and product groups. We will continue to ensure a truly collaborative approach to risk management with risk accountability sitting squarely with management and a proactive Group Risk function influencing decision making through effective challenge and timely consultation.

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### 2019 RISK MANAGEMENT TIMELINE

<table>
<thead>
<tr>
<th>Q1 2019</th>
<th>Q2 2019</th>
<th>Q3 2019</th>
<th>Q4 2019</th>
<th>Q1 2020</th>
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<tbody>
<tr>
<td><strong>INTERNAL AUDIT</strong></td>
<td></td>
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<tr>
<td>Risk Management Effectiveness Review report to Audit Committee</td>
<td>2020 Risk Based Internal Audit Plan Preparation</td>
<td></td>
<td>Risk Management Effectiveness Review report to Audit Committee</td>
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<td><strong>GROUP RISK TEAM</strong></td>
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<td></td>
<td>Report to Audit Committee</td>
<td>Prepare Review of Principal Risks</td>
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<td></td>
<td>Facilitate ‘top down’ review process</td>
<td>Report to Audit Committee</td>
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<tr>
<td><strong>BUSINESS RISK AREAS</strong></td>
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<tr>
<td>Quarterly Risk Review by leadership teams</td>
<td>Quarterly Risk Review by leadership teams</td>
<td>Quarterly Risk Review by leadership teams</td>
<td>Quarterly Risk Review by leadership teams</td>
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<tr>
<td>Review Principal Risks and map to Strategic Imperatives</td>
<td>Risk Register refresh and submission to Group Risk Team annual certification</td>
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<tr>
<td><strong>EXECUTIVE COMMITTEE</strong></td>
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<tr>
<td>Review reports from Group Risk Team</td>
<td>Review reports from Group Risk Team</td>
<td>‘Top Down’ review of Principal Risks</td>
<td>Review reports from Group Risk Team</td>
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<td></td>
<td></td>
<td>Approve Principal Risks</td>
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<td><strong>AUDIT COMMITTEE</strong></td>
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<tr>
<td><strong>BOARD</strong></td>
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<tr>
<td>Approve Principal Risks</td>
<td>Review of Principal Risks</td>
<td>Approve Principal Risks</td>
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</tbody>
</table>
During the year, the Board has carried out a robust assessment of the Principal Risks which could threaten the business model. These risks and the actions being taken to manage or mitigate them are explained in detail on pages 41–49 of this Annual Report.

In reaching our Viability Statement conclusion, we have undertaken the following process:

– The Audit Committee reviewed the Risk Management process at their meetings in February, July, September and December, receiving presentations from the Group Risk function, explaining the processes followed by management in identifying and managing risk throughout the business.

– In October, a series of detailed one-to-one discussions were held with each member of the Executive Committee and the Group Risk Team. In these discussions, the Executives were asked to consider the significant risks which they believed could seriously impact the profitability and future prospects of the Company and the principal risks that would threaten its business model, future performance, solvency or liquidity.

– As part of the strategy business updates in September, the Board considered and discussed the Principal Risks which could impact the business model over the next three years and discussed with the management team how these risks were being managed and mitigated.

– Throughout the year, a number of ‘deep dives’ and reviews into different risks were conducted by the Board, the Audit Committee and the Ethics & Compliance Committee looking into the nature of the risks and how they were mitigated, as detailed on page 48 of this Annual Report.

– Throughout the year, a number of ‘deep dives’ into specific risk areas were conducted by the Group Risk Team, the results of which were presented to and discussed by the Audit Committee and are detailed on page 48 of this Annual Report.

ASSESSMENT PERIOD

The Board have determined that the three-year period to December 2021 is an appropriate period over which to provide its Viability Statement. This period is aligned to the Group’s Strategic Planning process and reflects the Board’s best estimate of the future viability of the business.

SCENARIO TESTING

For the purpose of testing the viability of the Company, we have undertaken a robust scenario assessment of the principal risks and some other risks, which could threaten the viability or existence of the Company. These have been modelled as follows:

– In carrying out scenario modelling of the principal and significant risks on the following page we have also evaluated the impact of a severe but plausible combination of these risks actually occurring over the three-year period. We have considered and discussed a report setting out the terms of our current financing arrangements and potential capacity for additional financing should this be required in the event of one of the scenarios modelled occurring.

– We are satisfied that we have robust mitigating actions in place as detailed on pages 42–47 of this Annual Report. We recognise, however, that the long-term viability of the Company could also be impacted by other, as yet unforeseen, risks or that the mitigating actions we have put in place could turn out to be less effective than intended.
### 2018 SCENARIOS MODELLLED

#### SCENARIO 1 – PRICING AND REIMBURSEMENT PRESSURES

- **Pricing and reimbursement pressures or currency exchange volatility (Principal Risk)** – leading to a major loss of revenues and profits.

  - **Action taken:** We have modelled a 1% annual price erosion from 2019.

- **Link to strategy**
  - Achieve the full potential of our portfolio

- **Link to Principal Risks**
  - Pricing and Reimbursement

#### SCENARIO 2 – OPERATIONAL RISK

- **Execution risk** – our inability to launch new products losing significant market share to the competition.

  - **Action taken:** We have modelled a universal 1% reduction of annual volume growth from 2019.

- **Product liability claims** – giving rise to significant claims and legal fees.

  - **Action taken:** We have modelled a one-off significant product liability claim in 2020, without any insurance coverage.

- **Temporary loss of key production capability** – resulting in our inability to manufacture a key product for a period of time.

  - **Action taken:** We have modelled the loss of a factory, resulting in the loss of production and sales of a key product for two years from 2020.

- **Link to strategy**
  - Become the best owner
  - Transform the business through enabling technologies
  - Achieve the full potential of our portfolio

- **Link to Principal Risks**
  - New Product Innovation, Design & Development Including Intellectual Property
  - Commercial Execution
  - Business Continuity and Business Change

#### SCENARIO 3 – LEGAL REGULATORY AND COMPLIANCE RISKS

- **Regulatory measures** – impacting our ability to continue to sell key products.

  - **Action taken:** We have modelled the complete loss of revenue from a key product for each year from 2019.

- **Bribery and corruption claims** – giving rise to significant fines.

  - **Action taken:** We have assumed a one-off significant fine in 2020.

- **Link to strategy**
  - Become the best owner

- **Link to Principal Risks**
  - Legal and Compliance
  - Quality and Regulatory

#### SCENARIO 4 – CYBER SECURITY

- **Inability to issue invoices or collect money for a period of time.**

  - **Action taken:** We have modelled one of our key regions being unable to invoice for a month in 2020 due to an IT disruption.

- **Link to strategy**
  - Transform the business through enabling technologies

- **Link to Principal Risks**
  - Cyber Security

#### OTHER

- **Political and economic risk** – for example, political upheaval, which could cause us to withdraw from a major market for a period of time.

  - **Action taken:** We have modelled a major disruption due to a hard Brexit having a regulatory impact, and also causing severe delays with imports and exports for three months.

- **Link to strategy**
  - Become the best owner

- **Link to Principal Risks**
  - Political and Economic

---

### VIABILITY STATEMENT

Having assessed the principal risks, the Board has determined that we have a reasonable expectation that the Company will be able to continue in operation and meet its liabilities as they fall due over a period of three years from 1 January 2019. In our long-term planning we consider horizons of both five and ten years. However, as most of our efforts are focused on the coming three years, we have chosen this period when considering our viability.

Our conclusion is based on our current Strategic Plan approved by the Board in February 2019, having regard to longer-term strategic intentions, yet to be formulated in detail. However, we operate in a changing marketplace, which might cause us to adapt our Strategic Plan. In responding to changing external conditions, we will continue to evaluate any additional risks involved which might impact the business model.

By order of the Board, on 21 February 2019.

Susan Swabey
Company Secretary