State-of-the-art medical technology still needs a highly skilled pair of hands to use it.
Smith & Nephew is a global medical technology business. We have leadership positions in our four chosen specialities:
- Orthopaedic Reconstruction
- Advanced Wound Management
- Sports Medicine
- Trauma & Extremities

This success is built upon our three values of:
- Innovation
- Trust
- Performance

*These sections and pages 95, 97 and 99 form the Directors’ Report.*
Our mission

Delivering advanced medical technologies that help healthcare professionals, our customers, improve the quality of life for their patients

<table>
<thead>
<tr>
<th>$4.4bn</th>
<th>$987m</th>
<th>$810m</th>
</tr>
</thead>
<tbody>
<tr>
<td>Revenue(^1) up 4%</td>
<td>Trading profit(^2) up 5%</td>
<td>Operating profit(^1) up 1%</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>76.9¢</th>
<th>61.7¢</th>
<th>27.4¢</th>
</tr>
</thead>
<tbody>
<tr>
<td>Adjusted earnings per share(^2) up 3%</td>
<td>Earnings per share down 23%</td>
<td>Dividends per share up 5%</td>
</tr>
</tbody>
</table>

1 The underlying percentage increases/decreases are after adjusting for the effect of currency translation and the inclusion of the comparative impact of acquisitions and exclusion of disposals.
2 Explanations of these non-GAAP financial measures are provided on pages 161 to 163.

You can read more about our financial performance in the financial review on page 36
We are investing more in R&D to provide our customers with greater innovation.
We delivered a good performance in 2013

Financial highlights

You can read more about our financial performance in the financial review on page 36.
Chairman’s statement

Dear Shareholder,

In 2013, Smith & Nephew generated good underlying revenue and trading profit growth. We continued to focus investment on growth opportunities and returned significant value to Shareholders through increased dividends and a share buy-back programme. Momentum increased throughout the year as we delivered on our strategy to reshape Smith & Nephew for the future.

Our revenue was $4,351 million, up 4% on an underlying basis. Advanced Wound Management delivered strong growth, led by Healthpoint Biotherapeutics, our major 2012 acquisition. Sports Medicine Joint Repair had another successful year, and we improved our performance in Orthopaedic Reconstruction.

Almost 13% of our revenues now come from emerging market countries, up from just over 8% in 2010. We were one of the first companies in our sector to focus on these markets. We are building sustainable businesses through the strategy of establishing direct relationships with customers, as well as developing tailored products. In 2013, we invested further in our existing teams and made acquisitions in Brazil, India and Turkey to strengthen our platform.

Our trading profit was up 5% on an underlying basis at $987 million. The trading profit margin of 22.7% met our expectations as we invested more in the emerging markets and in research & development, and cost of the US medical device excise tax ($24 million in 2013).

Ethics, compliance & governance

We give high priority to compliance and ethics, as well as health, safety and the environment. The Board continues to encourage management in their drive to ensure all of Smith & Nephew’s programmes are world-class.

The Board also places great emphasis on governance and is mindful of its responsibility to promote the long-term interests of the Company for all our stakeholders. This is described in detail in the Corporate Governance section of this Annual Report (pages 44 – 85).

Creating sustainable value

Smith & Nephew has a long track record of creating value for Shareholders. For instance, we have paid a dividend every year since 1937. Since 2006, during my tenure as Chairman, it is pleasing to report that we have delivered a compound annual growth rate in adjusted earnings per share of 8% against a FTSE 100 average of 6%, along with a dividend compound growth rate of 14%. And the share price is up more than 90% in that time. The Group generated trading cash flow of $5.9 billion between 1 January 2006 and 31 December 2013, demonstrating our vitality over the long-term.

In 2013, we set out a Capital Allocation Framework that will govern how we prioritise the use of the strong cash flow we generate. This framework will guide our continued investment in organic growth, and maintenance of a progressive dividend. It also gives us headroom to make further acquisitions and includes a commitment to return any excess capital to Shareholders. It is underpinned by a desire to maintain a strong balance sheet to ensure solid investment grade credit metrics.

Following these principles, we spent $226 million on a share buy-back programme during the year. This, together with the 2012 dividend increase, resulted in a total distribution to Shareholders in 2013 of $465 million, two and a half times the level of the prior year.

The Board is pleased to propose a final dividend for the year of 17.0¢ per share, giving a total dividend for 2013 of 27.4¢, up 5% year-on-year.

Board changes

I will step down as Chairman of Smith & Nephew at the Annual General Meeting in April 2014. Roberto Quarta joined the Board as Non-executive Director in December 2013 and will take over as Chairman. Roberto has impressive business and board experience and is chairman of WiL pic, a FTSE 100 listed engineering business and of Clayton, Dubilier & Rice, Europe, a private equity firm.

Our Senior Independent Non-executive Director, Richard De Shutter, and Non-executive Director Ajay Piramal, will also both retire at the Annual General Meeting. I would like to thank them for their service. In particular, Richard’s contribution in this most important role has been invaluable. We are fortunate to have as replacement the highly experienced Brian Larcombe, who will become Senior Independent Non-executive Director.

In 2013, we welcomed to the Board Julie Brown as Chief Financial Officer and Michael Friedman as Non-executive Director. Julie has quickly established herself as an effective Executive Director and her influence is already seen in many areas, including the Capital Allocation Framework. Michael’s expertise in the US healthcare system and experience leading a major research and treatment institution has enhanced the Board.

Setting Smith & Nephew apart

During 2013, I was reminded of the quality of our people as we reviewed our responses to natural disasters, providing resources to aid recovery in the Philippines and in our own offices and communities, under Olivier Bohuon’s leadership, responding to a major flood at the Advanced Wound Management site in Hull, UK and to a tornado near our facility in Oklahoma City, US. The tenacity and compassion sets Smith & Nephew apart, as it has throughout our history of supporting healthcare professionals for more than 150 years.

It has indeed been a privilege working with the people at Smith & Nephew and to serve the interests of customers, employees and Shareholders. The Company has shown great resilience in the recent economic environment, building services for customers and value for Shareholders. There is an excellent team in place, both Executive and Non-executive.

I wish the Company well for a promising future.

Yours sincerely,

Sir John Buchanan
Chairman
We are operating in growth markets

Smith & Nephew today

TOTAL SEGMENT VALUE

ADVANCED SURGICAL DEVICES
$23.2bn  +4%

ADVANCED WOUND MANAGEMENT
$7.0bn  +4%

GLOBAL POPULATION

2.5 billion people  6 billion people  10 billion people

Our products are used by surgeons and nurses to help repair and heal the human body throughout a person's life.


You can read more about our financial performance in the marketplace review on page 16.
With a business model that creates value

OUR MISSION STATEMENT

Delivering advanced medical technologies that help healthcare professionals, our customers, improve the quality of life for their patients

OUR VALUES

Innovation  Trust  Performance

OUR STRATEGIC PRIORITIES

1. ESTABLISHED MARKETS
2. EMERGING & INTERNATIONAL MARKETS
3. INNOVATE FOR VALUE
4. SIMPLIFY AND IMPROVE OUR OPERATING MODEL
5. SUPPLEMENT ORGANIC GROWTH WITH ACQUISITIONS

You can read more about our strategy on page 12

OUR VALUE CREATION PROCESS

Research & Development  Regulatory & Compliance  Manufacturing  Medical Education  Sales & Marketing

You can read more about our business model on page 19

ATTRIBUTABLE PROFIT

$556m

OUR CAPITAL ALLOCATION FRAMEWORK

Reinvest for organic growth  Progressive dividend policy  Acquisitions in-line with strategy  Return excess to shareholders

Maintain a strong balance sheet to ensure solid investment grade credit metrics

You can read more about our Capital Allocation Framework on page 14

RESOURCE UTILISED

$5.8bn  $231m  11,036  14  $265m

Total Assets  Investment in R&D  Employees  Manufacturing plants worldwide  Corporation tax paid
We are organised by our areas of expertise

**Advanced Surgical Devices**

**ORTHOPAEDIC RECONSTRUCTION**
Specialist hip and knee implant systems.

**REVENUE**

<table>
<thead>
<tr>
<th>Year</th>
<th>Revenue (m)</th>
<th>% Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>2012</td>
<td>$1,540m</td>
<td></td>
</tr>
<tr>
<td>2013</td>
<td>$1,518m</td>
<td>-1%</td>
</tr>
</tbody>
</table>

**TRAUMA & EXTREMITIES**
Internal and external devices used in the stabilisation of severe fractures and deformity correction procedures.

**REVENUE**

<table>
<thead>
<tr>
<th>Year</th>
<th>Revenue (m)</th>
<th>% Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>2012</td>
<td>$474m</td>
<td></td>
</tr>
<tr>
<td>2013</td>
<td>$486m</td>
<td>+4%</td>
</tr>
</tbody>
</table>

**SPORTS MEDICINE JOINT REPAIR**
Instruments, technologies and implants necessary to perform minimally invasive surgery of joints.

**REVENUE**

<table>
<thead>
<tr>
<th>Year</th>
<th>Revenue (m)</th>
<th>% Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>2012</td>
<td>$474m</td>
<td></td>
</tr>
<tr>
<td>2013</td>
<td>$496m</td>
<td>+7%</td>
</tr>
</tbody>
</table>

**ARTHROSCOPIC ENABLING TECHNOLOGIES**
Cutting, visualisation and fluid management technologies necessary for Sports Medicine Joint Repair.

**REVENUE**

<table>
<thead>
<tr>
<th>Year</th>
<th>Revenue (m)</th>
<th>% Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>2012</td>
<td>$458m</td>
<td></td>
</tr>
<tr>
<td>2013</td>
<td>$441m</td>
<td>-2%</td>
</tr>
</tbody>
</table>

**OTHER ASD**
Including gynaecological instrumentation.

**REVENUE**

<table>
<thead>
<tr>
<th>Year</th>
<th>Revenue (m)</th>
<th>% Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>2012</td>
<td>$162m</td>
<td></td>
</tr>
<tr>
<td>2013</td>
<td>$74m</td>
<td>+14%</td>
</tr>
</tbody>
</table>

**Advanced Wound Management**

**ADVANCED WOUND CARE**
Products for the treatment of acute and chronic wounds, including leg, diabetic and pressure ulcers, burns and post-operative wounds.

**REVENUE**

<table>
<thead>
<tr>
<th>Year</th>
<th>Revenue (m)</th>
<th>% Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>2012</td>
<td>$849m</td>
<td></td>
</tr>
<tr>
<td>2013</td>
<td>$843m</td>
<td>+1%</td>
</tr>
</tbody>
</table>

**ADVANCED WOUND DEVICES**
Traditional and single-use Negative Pressure Wound Therapy (‘NPWT’) and hydrosurgery systems.

**REVENUE**

<table>
<thead>
<tr>
<th>Year</th>
<th>Revenue (m)</th>
<th>% Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>2012</td>
<td>$180m</td>
<td></td>
</tr>
<tr>
<td>2013</td>
<td>$213m</td>
<td>+20%</td>
</tr>
</tbody>
</table>

**ADVANCED WOUND BIOACTIVES**
Bioactive technologies that provide unique approaches to debridement and dermal repair and regeneration.

**REVENUE**

<table>
<thead>
<tr>
<th>Year</th>
<th>Revenue (m)</th>
<th>% Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>2012</td>
<td>$N/A</td>
<td></td>
</tr>
<tr>
<td>2013</td>
<td>$280m</td>
<td>+47%</td>
</tr>
</tbody>
</table>
With over 11,000 employees supporting healthcare professionals globally

**US**

Our ASD head office is based in Andover and we have manufacturing facilities in Memphis, Mansfield and Oklahoma.

**EMPLOYEES**

4,640

**CONTINENTAL EUROPE**

Our main Continental European manufacturing facilities are in Tuttlingen – Germany and Aarau – Switzerland.

**EMPLOYEES**

1,986

**UK & IRELAND**

Home of our Global Head Office in London and our Advanced Wound Management Head office in Hull.

**EMPLOYEES**

1,664

**REST OF THE WORLD**

We have manufacturing facilities, warehouses and offices across the world to serve our customers.

**EMPLOYEES**

1,827

**CHINA**

Generated 30% revenue growth in 2013 and now our sixth largest country. We have manufacturing facilities in Beijing and Suzhou.

**EMPLOYEES**

919

**Brazil**

acquisition of Advanced Wound Management distribution.

**Turkey**

acquisition of Advanced Surgical Devices distribution.

**India**

acquisition of Sushrut-Adler including mid-tier trauma portfolio.
Dear Shareholder,

For more than 150 years Smith & Nephew has supported healthcare professionals as they improve the quality of life for patients. Today we do this by providing advanced medical technologies that move clinical boundaries and reduce economic costs.

We focus where we see developing needs and invest in new products and techniques to improve outcomes and expand access. Through these actions we are at the forefront of fast growing segments such as Sports Medicine and Advanced Wound Bioactives, are leaders in the emerging markets, and continue to develop in our more mature segments. We are building a sustainable business to best support surgeons, nurses and healthcare managers in the future.

In 2013, I am pleased to report that we made significant progress, expanding our product portfolio, building our platform, growing in the emerging markets and embedding a culture of perpetual efficiency.

Accelerating innovation

In 2013, we maintained a high rate of innovation, launching major new products such as the natural-motion JOURNEY™ II BCS Total Knee System and, in Sports Medicine, HEALICOIL™ REGENESORB™, an innovative next generation bio-composite suture anchor. We also delivered 23 new Advanced Wound Management products, such as the DURAFIBER® Ag antimicrobial dressing.

Looking ahead, we have a strong product pipeline, particularly in Trauma & Extremities and Sports Medicine. Overall we increased research & development (R&D) investment to $231 million in 2013, representing 5.3% of revenue, and are committed to maintaining these high levels of investment and innovation going forward. We were proud to be named one of Forbes Magazine’s ‘Most Innovative Companies’ of 2013.

We are also investing in medical education to ensure that our customers continue to have access to the best training on our products and techniques. This includes significant online resources such as Education and Evidence. Launched in 2013, this is a powerful new e-learning platform for surgeons to access and share peer-to-peer education.
so that ever more of our business comes from areas of higher growth

Healthpoint acquisition delivers
Our major acquisition at the end of 2012, Healthpoint Biotherapeutics, has given us a leading position in bioactives, the fastest growing segment of Advanced Wound Management. This business has outperformed our expectations, increasing its revenue by 47% in 2013. With its unique portfolio, excellent sales execution and expertise in product research and development, it is an outstanding addition to Smith & Nephew.

Leaders in emerging markets
Throughout 2013, we have built upon our leading position in the emerging markets, generating strong revenue growth. We enhanced our platform, investing in the sales force and infrastructure in markets such as Mexico and the Middle East, as well as acquiring distributors in Turkey and Brazil. By having a direct relationship with our customers we are able to offer them a fuller range of products and services.

We see a major opportunity to create portfolios for patients in the economic mid-tier across the emerging markets, and launched our first products and acquired the Sushrut-Adler Indian trauma business in 2013.

Perpetual efficiency
These strategic investments and many other initiatives have been made possible through our continued drive to be more efficient, to reduce cost, and to simplify and improve our operating model. In 2011, we announced an initial programme to generate annual savings of $150 million and this will be largely complete by the end of 2014. We are now a leaner business, and, as importantly, we are embedding a culture of perpetual efficiency into our processes and future thinking.

Sustainability
Our mission at Smith & Nephew is to help our customers improve people’s lives. I can think of nothing more intrinsic to this mission than operating sustainably and responsibly to deliver long-term benefits. In 2013, we maintained our commitment to our customers, patients, employees, communities and Shareholders. This was again recognised in our inclusion in the FTSE4Good and Dow Jones Sustainability indices.

Sir John Buchanan
Sir John Buchanan will step down as Chairman of the Board in April 2014. I wish to thank Sir John for his leadership, counsel and dedication over the past nine years. As Chairman he has overseen a number of significant changes and has given me tremendous support in my role as Chief Executive Officer. We are confident that in Roberto Quarta we have found another excellent Chairman.

Acquisition of ArthroCare Corp
In February 2014, we announced our intention to acquire ArthroCare, an innovative medical devices company with a highly complementary sports medicine franchise. Based in Austin, Texas, ArthroCare’s technology and products will significantly strengthen our portfolio – and we will use our global footprint to drive substantial new revenue growth. We expect to complete this acquisition in the middle of 2014 for a net cost of approximately $1.5 billion.

Rebalancing Smith & Nephew
Smith & Nephew made excellent progress in 2013, delivering both revenue and earnings growth and generating strong cash flow. I would like to thank our employees for their contribution during the year. It was their dedication and focus that achieved these results, and importantly, are enabling us to accomplish our programmes to make the Group fit and effective for the future.

We are successfully reshaping and rebalancing Smith & Nephew so that even more of our business comes from areas of higher growth. In this way we will continue to deliver the best support for our customers and the greatest value for our Shareholders.

Yours sincerely,

Olivier Bohuon
Chief Executive Officer
1 ESTABLISHED MARKETS

PERFORMANCE
Our businesses in the Established Markets grew by 5% in the US and was flat in the Other Established Markets, where the macro-economic environment in Europe continues to be weak.

By franchise, our performance relative to estimated global segment growth was slightly below in hip and knee reconstruction and trauma, around market in the higher growth joint repair segment of sports medicine and well above in advanced wound management. Hip and Knee Implant performance in 2013 was held back by our relatively high exposure to the weak European market, our position in the product cycle and metal-on-metal hip headwinds.

Our performance in the second half of 2013 was better than the first half, as a result of our investments in marketing, medical education and new products.

For more detail on the market and competition see pages 16 to 18.

GLOBAL OUTLOOK
Established Markets for Smith & Nephew are the US, Europe, Japan, Australia, New Zealand and Canada.

In these markets we expect the challenging economic conditions to continue, requiring realigned business models and focused investment, albeit that there are some signs of improvement in the US.

2 EMERGING & INTERNATIONAL MARKETS

PERFORMANCE
The Emerging & International Markets grew at 18%, exceeding Established Markets rates and contributing half of annual revenue growth for the Group.

These geographies now represent 13% of the Group’s overall revenue.

During 2013:
- Our success in China continued with growth of over 30% and now it is our 6th largest country by revenue.
- Significant investment to drive growth organically (e.g. Mexico and Saudi Arabia) and through acquisitions (Brazil, Turkey, India).
- We put in place our strategy to address the mid-tier market.

GLOBAL OUTLOOK
Emerging & International Markets represent those outside of the Established Markets including Brazil, China, India and Russia.

The healthcare environment in these markets is rapidly expanding and with the right investments offers significant opportunities for the Group.
3 INNOVATE FOR VALUE

PERFORMANCE
R&D investment now represents 5.3% of revenue, an increase in spending of 35% in reported terms. We have maintained our strong momentum of introducing new products:

- In ASD, we successfully launched the JOURNEY II BCS Knee System and our Sports Medicine franchise expanded through a next generation HEALICOIL suture anchor range and we also expanded our Extremities offering
- Over 20 new AWM products launched

GLOBAL OUTLOOK
Innovation offers the key to meeting the realities of healthcare and economic paradigm in both Established and Emerging & International Markets. New products, technologies and surgical techniques hold the potential of reducing the overall cost of healthcare.

R&D EXPENDITURE \( \text{AS A PERCENTAGE OF GROUP REVENUE} \)

\[
\begin{array}{ccc}
\text{Year} & \text{Amount} & \text{Percentage} \\
2011 & 167 & 3.9 \\
2012 & 171 & 4.1 \\
2013 & 181 & 5.3 \\
\end{array}
\]

4 SIMPLIFY AND IMPROVE OUR OPERATING MODEL

PERFORMANCE
Trading profit grew by 5% and trading profit margin decreased slightly to 22.7% as expected. Targeted investments, increased R&D and the new US Medical Device tax were partially off-set by efficiency and cost initiatives.

Key initiatives included:
- Continuing to deliver our $150 million per annum efficiency savings programme
- Expansion of the Suzhou facility continues on track
- Started roll-out of major Europe-wide single IT and business intelligence platform

GLOBAL OUTLOOK
By simplifying and improving our operating model we can liberate resources to invest in growth opportunities and meet the persistent price pressure. A simpler and more efficient organisation allows us to make faster and better decisions.

TRADING PROFIT \( \text{AS A PERCENTAGE OF GROUP REVENUE} \)

\[
\begin{array}{ccc}
\text{Year} & \text{Amount} & \text{Margin} \\
2011 & 961 & 22.5 \\
2012 & 965 & 23.3 \\
2013 & 1069 & 24.4 \\
\end{array}
\]

5 SUPPLEMENT ORGANIC GROWTH WITH ACQUISITIONS

PERFORMANCE
2013 has been another active year from a business development perspective, mainly focused on supporting our Emerging & International Markets strategy:

- Acquisition of distributors in Brazil and Turkey
- Acquisition of a mid-tier trauma business in India
- Successful integration of Healthpoint Biotherapeutics which we acquired in 2012

GLOBAL OUTLOOK
Acquisitions and partnerships are important elements which supplement organic investment and provide increased opportunity for high growth and value creation.

\[1\text{ The underlying percentage increases/decreases are after adjusting for the effect of currency translation and the inclusion of the comparative impact of acquisitions and exclusion of disposals.} \]

\[2\text{ Explanations of these non-GAAP financial measures are provided on pages 161 to 163.} \]
Dear Shareholder,

When I joined Smith & Nephew in February 2013 I found a business with a unified sense of purpose – helping customers to improve the quality of life of patients – and a clear strategy to deliver this in a sustainable manner across our Established and Emerging & International Markets. The management team were making choices about where to invest to maximise our impact today and to ensure Smith & Nephew has the products and platform for the future.

For me, the role of Finance is as a strategic partner, enabling and supporting the business as it makes investments and drives efficiencies, and ensuring we can maintain our financial strength and discipline. I believe Smith & Nephew has made significant progress in 2013 and that judicious financial management has been and remains central to our success.

Strong revenue and earnings

For the full year 2013, we generated good underlying revenue and trading profit growth and met our margin expectations. Revenue was $4,351 million, an underlying 4% increase. Trading profit was $987 million, up 5% underlying. The trading profit margin was 22.7% a reduction of 60bps. Our adjusted earnings per share were 76.9¢, up 3%. The trading cash flow was $877 million, reflecting a trading profit to cash conversion ratio of 89%.

Capital Allocation Framework

We consider that the efficient use of capital on behalf of Shareholders is an important objective. We have delivered good revenue and earnings growth and strong cash generation in the challenging markets of the last few years.

During 2011, we announced our Strategic Priorities, focusing our business on liberating resources to invest in driving greater growth. In order to support this strategy, the Board believes in maintaining an efficient, but prudent, capital structure, while retaining the flexibility to make value enhancing acquisitions. This approach was set out in the new Capital Allocation Framework announced in May 2013.

The Capital Allocation Framework will be 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.

This is underpinned by maintaining leverage ratios commensurate with solid investment grade credit metrics.

OUR CAPITAL ALLOCATION FRAMEWORK

- Reinvest for organic growth
- Progressive dividend policy
- Acquisitions in-line with strategy
- Return excess to Shareholders

Maintain a strong balance sheet to ensure solid investment grade credit metrics.
In-line with the above framework, and reflecting our confidence in the successful execution of our Strategic Priorities, we commenced a $300 million share buy-back programme in May 2013. As of 31 December 2013 we had spent $226 million. This programme was suspended following our agreement to acquire ArthroCare, announced on 3 February 2014.

Liberating resources
In August 2011, Smith & Nephew announced a programme to drive structural efficiencies in order to liberate the resources needed to fund investment in the emerging markets and R&D, targeting savings of at least $150 million per annum. The cost of the currently identified programmes is expected to be $160 million in cash and $40 million in non-cash costs. To date the Group has realised annualised benefits of $131 million and we expect to complete the programme in early 2015 and realise slightly more than the anticipated benefits. The costs are on track. As a result of this programme and other actions, a culture of continuously looking to be more efficient is being embedded across the Group.

Acquisitions
During the year the Group has completed acquisitions of manufacturing and distribution businesses in Turkey, Brazil and India. The aggregate cost was $126 million. Through these acquisitions, we are implementing a number of our Strategic Priorities: to build leadership positions in the Emerging & International Markets; to supplement our organic growth through acquisitions; and to bring forward mid-tier portfolios to these countries.

Outlook
We anticipate the market conditions seen in the second half of 2013 to continue in 2014. We expect the US to be stable with some signs of improvement, Europe to remain challenging and the emerging markets to continue to offer opportunities for higher growth.

In terms of revenue growth by franchise, we expect:
- Orthopaedic Reconstruction, continuing its recent improved performance, to grow at approaching the market rate;
- Trauma & Extremities, building upon our recent investments, to grow overall at the market rate, but with a stronger second half to the year;
- Sports Medicine, with its strong product pipeline, to deliver growth above the market rate; and
- Advanced Wound Management, with its unique mix of leading products, to deliver another year of growth above the market. Within this, we expect Advanced Wound Bioactives to grow at a rate in the mid-teens.

In terms of trading profit margin, we expect to exceed our 2013 performance.

I am confident that our continuing focus on efficiency, coupled with further investments to drive growth and the disciplined use of our strong cash flow will generate greater value for our Shareholders.

Yours sincerely,

Julie Brown
Chief Financial Officer
Market trends
Demand for healthcare continues to increase worldwide influenced by the following trends:

Increased longevity and average age
As a result of improvements in healthcare and living conditions, life expectancy across the world has increased in modern times and this increase is expected to continue.

The Organisation for Economic Co-operation and Development (OECD) calculates the average life expectancy at birth in 2010 as 79.7, a significant rise from the 70.3 calculated in 1970.

As a consequence of longer life expectancy and the falling birth rates in many developed countries, there is an expanding gap between the demand for healthcare and the ability of governments to supply healthcare. Demand for healthcare will increase because of the ageing world population but at the same time the changing balance of age in the population means that, relatively speaking, there is potentially an accompanying decrease in funds available for healthcare raised through taxation of the working population.

More active lifestyles
Demand for healthcare is also increasing because people now expect to maintain active lifestyles longer into retirement and to return to activity sooner after treatment. This has resulted in a desire for less invasive surgery and quicker recovery times. Patients also desire products with a better replication of natural movement and an ability to cope with more rigorous activity over a longer period.

Obesity and associated chronic diseases
Obesity is an increasing global problem which causes more wear on the joints of the human body and increases demand for orthopaedic reconstruction.

Across the OECD countries, an average of 18% of the population is obese; this has increased from 13% in 2000.

Obesity also increases the risk of diabetes which can lead to other medical conditions and complications. In 2012, the International Diabetes Federation estimated that 8.3% of the world’s population (371 million people) suffer from diabetes and this is projected to rise to 9.9% (552 million people) by 2030.

There is a proven link between diabetes and a higher risk of surgical site infections which increases the risk of surgical procedures on diabetic patients. This risk can be minimised with the use of specialist wound care products designed to lower the risk of infection.

It is estimated that up to 10% of people with diabetes also suffer from diabetic foot ulcers. These ulcers are prone to infection, causing an increased risk of amputation, increased morbidity and are a significant burden on the health system.

Increased affluence in emerging markets
The emerging markets are becoming more affluent and therefore more able to afford medical treatments. However, the cost of many medical devices restricts access by the wider population.

Patient awareness
In certain countries, patients are becoming increasingly aware, from the internet and direct-to-customer advertising, of the various healthcare options and treatments available. This has led to some increased patient influence over the product purchasing decisions of medical service providers.

We operate in
dynamic markets

OECD COUNTRIES’ POPULATION

<table>
<thead>
<tr>
<th>The number of people aged 20-64 per person aged 65+</th>
<th>1950</th>
<th>2000</th>
<th>2050</th>
</tr>
</thead>
<tbody>
<tr>
<td>Source: OECD Social Indicators – Society at a Glance 2011</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Global economic crisis

The supply of healthcare in many of our markets is funded by governments. The global economic crisis in recent years has placed increased pressure on governments around the world to reduce or constrain healthcare expenditure.

In summary

The increased demand for healthcare products and the limitation of available resources is widening the funding gap. Providing technologies that deliver value by improving clinical outcomes while reducing the consumption of overall healthcare resources is vital for the success and sustainability of medical device businesses.

RESPONDING TO THE MARKET

Smith & Nephew is committed to developing products that respond to the demand and supply pressures faced by the healthcare industry. Some examples are set out below.

Our VERILAST\textsuperscript{\textcopyright} Technology has been laboratory tested to demonstrate wear performance sufficient for 30 years of use enabling a total replacement option for younger, more active patients.

PICO\textsuperscript{\textcopyright} is our single use NPWT product which brings the wound healing benefits of NPWT to a wider audience due to its discrete size and portability. Research is also proving the benefits of NPWT products to reduce recovery times after major surgery, such as caesarean sections.

VISIONAIRE\textsuperscript{\textcopyright}, our patient matched instrumentation, uses the patient’s MRI and X-rays to design cutting blocks specific to each patient. This may reduce surgery time by eliminating several sizing and alignment steps and improves precision in fitting the implant.

We are developing products targeting the middle economic tier of the emerging markets to capitalise on their forecast growth. This will enable doctors and nurses to deliver quality products to new patient communities around the world.

Regulatory standards and compliance in the healthcare industry

The international medical device industry is highly regulated. Regulatory requirements are important in determining whether substances and materials can be developed into marketable products and the amount of time and expense that should be allotted to such development.

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. Of particular importance is the requirement in many countries that products be authorised or registered prior to manufacture, marketing or sale and that such authorisation or registration be subsequently maintained. The major regulatory agencies for Smith & Nephew’s products include the Food and Drug Administration (FDA) in the US, the Medicines and Healthcare products Regulatory Agency in the UK, the Ministry of Health, Labour and Welfare in Japan and the China Food and Drug Administration.

In general, the trend in many countries in which we do business is towards higher expectations and increased enforcement activity by governmental authorities.

We are committed to doing business with integrity and welcome the trend to higher standards in the healthcare industry. We and other companies in the industry have been subject to investigations and other enforcement activity that have incurred and may continue to incur significant expense. See 'Legal proceedings' on page 130.
## Dependence on government and other funding

In most markets throughout the world, expenditure on medical devices is ultimately controlled to a large extent by governments. Funds may be made available or withdrawn from healthcare budgets as a result of government policy. We are therefore largely dependent on future governments providing increased funds commensurate with the increased demand arising from demographic trends.

Pricing of our products is largely governed in most developed markets by governmental reimbursement authorities. Initiatives sponsored by government agencies, legislative bodies and the private sector to limit the growth of healthcare costs, including price regulation, excise taxes and competitive pricing, are ongoing in markets where we operate. This control may be exercised by determining prices for an individual product or for an entire procedure. We are exposed to changes in reimbursement policy, tax policy and pricing which may have an adverse impact on revenue and operating profit. In particular, from 2013 changes to the healthcare legislation in the US have imposed significant taxes on medical device manufacturers. There may be an increased risk of adverse changes to government funding policies arising from the deterioration in macro-economic conditions in some of our markets.

## Competitors

Competition exists among healthcare providers to gain patients on the basis of quality, service and price. Providers are under pressure to reduce the total cost of healthcare delivery. In order to achieve this there has been some consolidation in our customer base, as well as amongst our competitors, and these trends are expected to continue in the long term. We compete against both local and multinational corporations, including some with greater financial, marketing and other resources.

Our competitors include Arthrex, Biomet, DePuy Synthes, Stryker and Zimmer in our Advanced Surgical Devices division and Coloplast, Convatec, Kinetic Concepts and Molnlycke in our Advanced Wound Management division.

## Customers

In certain parts of the world, including the UK, much of Continental Europe, Canada and Japan, the healthcare providers are largely government organisations funded by tax revenues. In the US, our major customers are public and private hospitals, which receive revenue from private health insurance and government reimbursement programmes. Medicare is the major source of reimbursement in the US, for knee and hip reconstruction procedures and for wound treatment regimes.

### MARKET SEGMENT AND LEADERSHIP

#### Hip & Knee Implants

<table>
<thead>
<tr>
<th>Manufacturer</th>
<th>Market Share</th>
<th>Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>Zimmer</td>
<td>23%</td>
<td>+3%</td>
</tr>
<tr>
<td>Smith &amp; Nephew</td>
<td>11%</td>
<td></td>
</tr>
<tr>
<td>Stryker</td>
<td>19%</td>
<td></td>
</tr>
<tr>
<td>Biomet</td>
<td>12%</td>
<td></td>
</tr>
<tr>
<td>Depuy Synthes</td>
<td>20%</td>
<td></td>
</tr>
</tbody>
</table>

#### Sports Medicine

<table>
<thead>
<tr>
<th>Manufacturer</th>
<th>Market Share</th>
<th>Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>Arthrex</td>
<td>28%</td>
<td>+6%</td>
</tr>
<tr>
<td>Smith &amp; Nephew</td>
<td>20%</td>
<td></td>
</tr>
<tr>
<td>Linvatec</td>
<td>5%</td>
<td></td>
</tr>
<tr>
<td>Depuy Mitek</td>
<td>15%</td>
<td></td>
</tr>
<tr>
<td>Biomet</td>
<td>4%</td>
<td></td>
</tr>
</tbody>
</table>

#### Trauma & Extremities

<table>
<thead>
<tr>
<th>Manufacturer</th>
<th>Market Share</th>
<th>Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>Zimmer</td>
<td>6%</td>
<td>+7%</td>
</tr>
<tr>
<td>Smith &amp; Nephew</td>
<td>10%</td>
<td></td>
</tr>
<tr>
<td>Stryker</td>
<td>22%</td>
<td></td>
</tr>
<tr>
<td>Biomet</td>
<td>6%</td>
<td></td>
</tr>
<tr>
<td>Depuy Synthes</td>
<td>47%</td>
<td></td>
</tr>
</tbody>
</table>

#### Advanced Wound Management

<table>
<thead>
<tr>
<th>Manufacturer</th>
<th>Market Share</th>
<th>Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>Smith &amp; Nephew</td>
<td>20%</td>
<td>+4%</td>
</tr>
<tr>
<td>Coloplast</td>
<td>15%</td>
<td></td>
</tr>
<tr>
<td>Convatec</td>
<td>8%</td>
<td></td>
</tr>
<tr>
<td>Kinetic Concepts</td>
<td>19%</td>
<td></td>
</tr>
<tr>
<td>Molnlycke</td>
<td>12%</td>
<td></td>
</tr>
</tbody>
</table>

* Data: 2013 estimates generated by Smith & Nephew based upon public sources and internal analysis.
  * Representing access, resection and repair products.
  ** A division of Johnson & Johnson.
Our mission is to deliver advanced medical technologies

Improving quality of life

Smith & Nephew’s business model, set out on page 7, supports our mission to deliver advanced medical technologies to help healthcare professionals, our customers, improve the quality of life for their patients.

Through it we:
- invest in research & development to create innovative new solutions that improve clinical outcomes and reduce the economic burden on healthcare systems;
- rigorously enforce regulatory and compliance standards, conducting business ethically everywhere we operate;
- ensure our manufacturing, supply and distribution footprint is lean and efficient;
- provide medical education and product training to healthcare professionals to help ensure safe and effective treatment for patients; and
- support our sales and marketing teams to guarantee our customers have the advanced technologies and supporting services they need to treat their patients.

Our business model is underpinned by our values and Capital Allocation Framework:
- our values of Innovation, Trust and Performance focus our people on being responsive to the needs of our customers, energetic, creative and passionate in our work, and building lasting and close relationships with our stakeholders; and
- Our Capital Allocation Framework enables us to invest for the future, both in organic growth and through acquisitions, whilst also generating value for Shareholders today through a progressive dividend policy and commitment to return any excess capital.

By implementing our Strategic Priorities we increase momentum throughout the business model to:
- build on our strong position in the Established Markets;
- realise the significant opportunities in the Emerging & International Markets;
- maintain an unrelenting focus to innovate for value;
- simplify and improve our operating model to maximise efficiency; and
- supplement our organic growth through acquisitions.

Research and development

We have a deep knowledge of the needs of surgeons and nurses, we understand the economic pressures healthcare payers work under, and we recognise that patients are demanding better treatment options to restore quality of life. These factors inform our research and development (‘R&D’) strategy, which is at the heart of our business model.

In 2013, we again delivered many new and innovative products. Those included a major new knee platform, the JOURNEY II BCS, the first sports medicine product to use Smith & Nephew’s proprietary advanced bicomposite material in the HEALICOIL REGENESORB Suture Anchor; and DURAFIBER Ag, combining a highly absorbent, gelling fibre dressing with the antimicrobial benefits of silver.

We have a strong new product pipeline for 2014, with many innovations scheduled, in particular in Sports Medicine Joint Repair, Trauma and Advanced Wound Management. These new products, and many more currently in development, are a result of our focus on R&D. We invested $231 million in this area in 2013. At 5.3% of revenue this is an increase from the 4.1% spent in the previous year. We expect to maintain our investment level at around 5% of revenue going forward.

We are highly disciplined in project selection. Our R&D experts in the UK, US, Europe, China and India have extensive customer and sector knowledge, which is augmented by ongoing interaction with our marketing teams. Strict criteria are applied to ensure new products fulfill an unmet clinical need, have a strong commercial case, and are technologically feasible. Our R&D teams also work closely with manufacturing and supply chain management to ensure we can produce new products to clinical, cost and time specification.

Open Innovation

As part of our R&D strategy, Smith & Nephew supports and works with numerous small companies looking for help with developing and commercialising new technologies.

As supporters of NASA’s TecFusion Open Innovation programme we access and support companies developing highly creative, often disruptive, technologies that are funded by the US federal government.

We are a primary sponsor of the Massachusetts Medical Device Development Center (‘M2D2’) New Venture Competition, supporting entrepreneurial product development by early-stage medical device companies.
Our business continued

We are the commercial partner in SWAN-iCare, an EU-funded initiative to bring multidisciplinary European research teams together to deliver a next generation integrated autonomous solution for monitoring and adapting personalised therapy of foot and leg ulcers.

InVentures
Smith & Nephew also welcomes new product concepts from surgeons. Through our InVentures programme we collaborate to bring ideas to reality. InVentures evaluates surgeon concepts for technical and market viability and our development team works hand-in-hand with surgeons to deliver new products that advance healing. Commercialised products benefit from the global selling power of Smith & Nephew.

In 2013, we introduced a new MODULAR RAIL SYSTEM for deformity correction and limb restoration that was designed in collaboration with Dror Paley MD through the InVentures programme. This new treatment option highlights our increased investment in extremities and limb restoration, and our commitment to working directly with surgeon inventors.

Intellectual property
We protect the results of our research and development through patents and other forms of intellectual property. The Group’s patent portfolio currently includes in excess of 5,000 patents and patent applications. Patent protection for our products is sought routinely in our principal markets.

We also have a policy of protecting our products by registering trademarks under the local laws of markets in which such products are sold. We vigorously protect our trademarks against infringement.

In addition to protecting our market position by filing and enforcing patents and trademarks, we may oppose third party patents and trademark filings where appropriate in those areas that might conflict with our business interests.

In the ordinary course of business, we enter into a number of licensing arrangements with respect to our products. None of these arrangements individually is considered material to our current operations and financial results.

Regulatory and compliance

Code of conduct and business principles
Smith & Nephew earns trust with patients, customers, healthcare professionals, authorities 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 distributors and independent agents that sell our products, as well as vendors that interact with others on our behalf. Our Code of Conduct and Business Principles (‘Code’) 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 Smith & Nephew operates. We are committed to upholding our promise in our Code that we will not retaliate against anyone who makes a report in good faith.

New employees receive training on our Code, and we assign annual compliance training to employees. In 2013, we created two additional courses: a refresher course on Preventing Bribery and Corruption and ‘Effective Communication’.

Global compliance programme
Smith & Nephew has implemented what we believe is a world-class Global Compliance Programme that helps our businesses manage risk and comply with laws and regulations. In 2013, Smith & Nephew continued to strengthen its comprehensive compliance programme, which includes global policies and procedures, on-boarding and annual training for its employees, managers, independent agents and key employees of distributors and high risk vendors around the world, monitoring and auditing processes, and reporting channels. Through a global intranet website, we provide resources and tools to guide employees to make decisions that comply with the law and our Code and earn trust. We conduct advance review and approval for any significant interactions with healthcare professionals or government officials. New distributors are subject to due diligence and are contractually obligated to comply with applicable laws and our Code. Their management are required to take compliance training and certify that they will ensure their employees and agents comply with the law and our Code. In 2013, we launched a compliance programme toolkit, in multiple languages, for our distributors to provide them with the resources to establish their own compliance programme. The toolkit includes draft policies, training materials and approval forms.

New treatment for venous leg ulcers
HP802-247 is an investigational human cell therapy for the treatment of venous leg ulcers currently in Phase III trials. Results from Phase IIb trials investigating the efficacy of HP802-247 were previously published in The Lancet.

Based on in vitro studies, HP802-247 is believed to release various growth factors and cytokines into the micro-environment of the wound. These living cells are anticipated to interact with the patient’s own cells to stimulate wound healing. HP802-247 has been designed to deliver a defined cell ratio (keratinocyte:fibroblasts) to support optimal tissue regeneration.

Venous leg ulcers are increasingly common and costly to healthcare systems and a cause of prolonged suffering for patients. These wounds are caused by swelling and inflammation secondary to blockage or backflow in the veins of the legs. Many venous ulcers fail to heal even after three months of standard treatment and develop into chronic, non-healing wounds.

Based on an estimated figure of 2.5 million venous leg ulcers in the United States alone and a study of actual direct treatment costs of $9,685 per person, the annual cost of treating these wounds is likely to be in the many billions of dollars. Accordingly, the availability of innovative and more effective treatment strategies for such high-risk wounds could provide tremendous benefits to both patients and society.
In 2012, under the terms of the Company’s Foreign Corrupt Practices Act (FCPA) settlement (see Note 17.3 of the Notes to the Group accounts), we retained an independent monitor to review the effectiveness of our compliance programme and make recommendations, as appropriate, for further enhancements to the programme. In collaboration with the independent monitor, our programme has been enhanced even further. In late 2013, the monitor completed his 18-month review and concluded that Smith & Nephew’s compliance programme is reasonably designed and implemented to detect and prevent violations of the anti-corruption laws and is functioning effectively. Smith & Nephew will report directly to the US Department of Justice (DOJ) and the US Securities and Exchange Commission (‘SEC’) for the remainder of the three-year settlement agreement.

Manufacturing

We continue to implement Lean Manufacturing throughout our factories and the supply chain to improve and sustain higher levels of service, quality, productivity and efficiency.

Core competencies include: materials technology; high-precision machining in Advanced Surgical Devices; and high-volume, automated manufacturing in Advanced Wound Management.

4 SIMPLIFY AND IMPROVE OUR OPERATING MODEL

Perpetual efficiency

The significant investments undertaken in 2013 have been possible through our successful drive to be more efficient, reduce cost, and simplify and improve our operating model.

In 2011, we announced a programme to generate annual savings of $150 million. As a result of our work to date, we have annualised benefits of $131 million. The programme will be largely complete by the end of 2014.

Significant actions included a major reorganisation when we created the Advanced Surgical Devices division, the opening of an extension to our Advanced Wound Management factory in Suzhou, China, and the introduction of a major new IT platform.

We are now a leaner business, and, as importantly, we are embedding a culture of perpetual efficiency into our processes and future thinking.

We purchase raw materials, components, finished products and packaging materials from certain key suppliers. These principally include metal forgings and stampings for orthopaedic products, optical and electronic sub-components and finished goods for sports medicine products, active ingredients and finished goods for Advanced Wound Management and packaging materials across all businesses. Suppliers are selected, and contracts negotiated, by a centralised procurement team wherever possible, with a view to ensure value for money based on the total spend across the Group.

We outsource manufacturing where necessary to obtain specialised expertise or where it is possible to gain lower cost without undue risk to intellectual property. Suppliers of outsourced products and services are selected based on their ability to deliver products and services to specification, and establish and maintain a quality system. Suppliers are trained and are monitored through on-site assessments and performance audits that include quality, service and delivery.

Finishing goods purchased for resale include screen displays, optical and electrical devices in the Advanced Surgical Devices division and skincare products in the Advanced Wound Management division.

We operate a number of manufacturing facilities around the globe, which are predominantly division specific, and a number of central distribution facilities in the key geographical areas in which we operate. Products are shipped to Group companies which hold small amounts of inventory locally for immediate or urgent customer requirements.

Advanced Surgical Devices

The Advanced Surgical Devices division’s largest manufacturing operation is based in Memphis (Tennessee, US), with additional production and assembly plants based in Mansfield (Massachusetts, US), Oklahoma City (Oklahoma, US), Aarau (Switzerland), Tuttinglen (Germany), Beijing (China), Calgary (Canada), Warwick (UK) and Sangametshwar (India).

The Memphis facilities produce key products and instrumentation in our Knee Implants, Hip Implant and Trauma franchises. These include the JOURNEY II LCS and LEGION® Knees, the ANTHOLOGY® Primary Hip System and key Trauma products such as the PERI-LOC® Ankle Fusion Plating System and TRIGEN® Intradural Nails. In addition to this, Memphis is the home to the design and manufacturing process of the VISIONAIRE Patient Matched Instrumentation Sets.

The Mansfield facility focuses on sports medicine related products for minimally invasive surgery including the FAST FIX® 360 Meniscal Repair System, FOOTPRINT® PK Suture Anchor, DYONICS® Platinum Shaver Blades, ENDOBUTTON® CL Ultra and the HEAUCOIL PK suture anchor. The Aarau, Tuttinglen, Beijing and Warwick facilities produce a large number of products including key Trauma products, the PLUS® knee and hip range and the BIRMINGHAM® Hip Resurfacing System. The facility in Oklahoma City deals mainly with the assembly of surgical digital equipment, such as HD560 Camera.

A distribution facility in Baar (Switzerland) serves as the main holding and consolidation point for markets in Europe. In the US, the distribution hub is located in Memphis.

Advanced Wound Management

Advanced Wound Management is headquartered in Hull (UK) which is home to a large proportion of the division’s manufacturing activities. There are also manufacturing facilities in Gilberdyke (UK), Suzhou (China), Curacao (Dutch Caribbean), Alberta (Canada) and Oklahoma City.

The products made at the Hull site cover the therapies of Exudate Management (Foam products – principally ALLEVYN®), Burns treatment (ACTICOAT®) and Wound Closure (OPSITE® film products). Several brands produced in Hull, such as JELONET® and BACTIGRAS®, will be transitioning to Suzhou in 2014.

A key base material used in the production of a large number of dressings is the intermediate bulk rolls of film which are manufactured in the Gilberdyke (UK) facility. The facility in Alberta (Canada) provides specific expertise in the addition of silver coatings onto the ACTICOAT burns range prior to shipping to Hull for the final conversion process into finished dressings.
The Suzhou facility opened in 2009 initially to manufacture some Foam products within Exudate Management. It has since expanded to take on production of some Film Wound Closure products.

NPWT is an area of the business which is growing strongly. The majority of the NPWT components are bought in from third parties and assembled in the Advanced Surgical Devices Oklahoma City facility, with the exception of the dressings used for the PICO product which are manufactured in Hull.

Manufacturing for Advanced Wound Bioactives takes place in Curacao, and at various third party facilities in the US. The products are distributed from a third party logistics facility in San Antonio, Texas.

Advanced Wound Management distribution hubs are located in Neunkirchen (Germany) and Derby (UK) for international distribution, Bedford (UK) for UK domestic distribution and Lawrenceville (Georgia, US) for US distribution.

Medical education

Smith & Nephew is dedicated to helping healthcare professionals improve the quality of care for patients. We are proud to support the professional development of surgeons and nurses by providing them with medical education and training on our Advanced Surgical Devices and Advanced Wound Management products.

Every year thousands of customers attend our state-of-the-art training centres in the US, UK and China and Smith & Nephew courses at multiple hospitals and facilities around the world. Working under expert guidance, attendees refine techniques and learn new skills, whilst experiencing the safe and effective use of our products. We also support healthcare professionals through our online resources such as the Global Wound Academy and, for surgeons, our Education and Evidence website.

Sales and marketing

Our customers are the providers of medical and surgical treatments and services in over 90 countries worldwide. The largest single customer worldwide is a purchasing group based in the UK that represented 6% of our worldwide revenue in 2013.

In our Established Markets, our Advanced Surgical Devices are principally shipped and invoiced directly to healthcare providers, hospitals and other healthcare facilities. Certain Advanced Wound Management products are shipped and invoiced to wholesale distributors and others are consigned to distributors that lease the devices to healthcare providers, hospitals and other healthcare facilities and end-users.

Each division operates its own dedicated sales force as the customer for the divisions’ products are usually different. Our US sales forces consist of a mixture of independent contract workers and employees. Sales agents are contractually prohibited from selling products that compete with our products. In most Other Established Markets, each division typically manages employee sales forces directly.

In our Emerging & International Markets we operate through direct selling and marketing operations, and through distributors. In these markets, our Advanced Surgical Devices franchises frequently share sales resources. The Advanced Wound Management sales force may be separate where it calls on different customers.

Our people

Smith & Nephew had over 11,000 employees in 2013. We are committed to attracting, engaging, developing and retaining employees as well as to being a responsible corporate citizen.

Our employees are dedicated to our core values of Innovation, Trust and Performance which represent the foundation of our culture.

Investing in our people and communities helps ensure the long-term sustainability of our business. In 2013, we executed actions to address employee feedback from our Global Survey and also participated in the Great Places to Work survey in many of our markets.

Attracting the best talent and developing and engaging our employees is critical to achieving and sustaining our business objectives and overall performance. Our appointments are made on merit and in alignment with a core set of competencies and values of which ethics and integrity are central. We prioritise the development and promotion of our employees whenever possible.
Each year, Smith & Nephew conducts a comprehensive global development and capability review process to identify high-potential employees and ensure they have career development plans in place. Talented employees are provided with opportunities to develop and grow their skills and career. Current programmes include the CEO Forum, designed to develop talent and provide exposure to the broader business, and the General Managers Meeting, held annually to align these key leaders with the Group’s strategy and goals. In addition, the Board reviews succession plans for key executive roles. We have succession plans for critical positions across our business and have taken proactive steps to recruit specialist and leadership talent to augment our current team.

Our performance management process ensures all employees set objectives which align to our overall business goals. Reward systems are focused on promoting high-performance and ethical behaviour. Our Code of Conduct is an important measure of individual performance. All employees are required each year to complete training and certify their adherence to this Code.

Smith & Nephew strives to create a more engaged and productive workforce and focuses on measures to drive employee engagement. These include an understanding of the Group’s mission and direction, sense of employee involvement, focus and adaptability to customers and market place. We continue to listen to our employees, via regular surveys and focus groups, and we value their opinions.

Diversity at Smith & Nephew

Smith & Nephew believes that diversity fuels innovation. We are committed to employment practices based on equality of opportunity, regardless of colour, creed, race, national origin, sex, age, marital status, sexual orientation or mental or physical disability unrelated to the ability of the person to perform the essential functions of the job.

The Board and Executive Officers continue to recognise the importance of diversity and over the last two years have expanded their own diversity profile. Three of our 12 Board members are female.

At 31 December 2013, Smith & Nephew had the following breakdown of employees:

<table>
<thead>
<tr>
<th>Category</th>
<th>Number of Employees</th>
</tr>
</thead>
<tbody>
<tr>
<td>Directors</td>
<td></td>
</tr>
<tr>
<td>Male</td>
<td>9</td>
</tr>
<tr>
<td>Female</td>
<td>3</td>
</tr>
<tr>
<td>Total</td>
<td>12</td>
</tr>
<tr>
<td>Senior Managers and above</td>
<td></td>
</tr>
<tr>
<td>Male</td>
<td>484</td>
</tr>
<tr>
<td>Female</td>
<td>140</td>
</tr>
<tr>
<td>Total</td>
<td>624</td>
</tr>
<tr>
<td>Total employees</td>
<td></td>
</tr>
<tr>
<td>Male</td>
<td>7,203</td>
</tr>
<tr>
<td>Female</td>
<td>4,821</td>
</tr>
<tr>
<td>Total</td>
<td>12,024</td>
</tr>
</tbody>
</table>

1 Number of employees as at 31 December 2013 including part time employees and employees on leave of absence.
2 Senior managers and above includes all employees classed as Directors, Senior Directors, Vice Presidents and Executive Officers and includes all statutory Directors of our subsidiary companies.
Advanced Surgical Devices

REVENUE 1 ($m)

+1% $3,015m

2009 2010 2011 2012 2013

TRADING PROFIT 1,3 ($m)

+2% $712m

2009 2010 2011 2012 2013

OPERATING PROFIT 1

+4% $620m

2009 2010 2011 2012 2013

TRADING PROFIT MARGIN 2

+20bps 23.6%

2009 2010 2011 2012 2013

MANUFACTURING SITES

- US and Canada: Memphis TN, Mansfield MA and Oklahoma City OK, Calgary – Canada
- Europe: Aarau – Switzerland, Tuttlingen – Germany
- UK: Leamington Spa (Warwick)
- Other: Beijing – China, Sangameshwar – India

SERVICE CENTRES

- US, UK, Germany, Japan and Australia

1 The underlying percentage increases/decreases are after adjusting for the effect of currency translation and the inclusion of the comparative impact of acquisitions and exclusion of disposals.
2 Explanation of these non-GAAP financial measures are provided on pages 161 to 163.
3 The 2012 revenue by franchise has been restated to 2013 product franchises.
Overview

In Advanced Surgical Devices (‘ASD’) we develop, manufacture and sell products in the following franchise areas:

Orthopaedic Reconstruction

Smith & Nephew offers a range of specialist products for orthopaedic reconstruction in its Knee Implants and Hip Implants franchises.

Implant bearing surfaces such as the proprietary OXINIUM® Oxidized Zirconium continue to be a point of differentiation for Smith & Nephew. OXINIUM Technology combines the enhanced wear resistance of a ceramic bearing with the superior toughness of a metallic bearing. When combined with highly cross-linked polyethylene (‘XLPE’) it results in our proprietary VERILAST Technology. In Hip Implants, the combination of a ceramicised metal head and a polyethylene lined cup have been shown in joint registry data to have superior five-year survivorship (97.9%) compared to implants made from any other material. In Knee Implants, the LEGION Primary Knee with VERILAST Technology is the only knee implant with a 30-year wear performance claim — more than double the length of wear performance testing of conventional technologies.

Knee Implants

Smith & Nephew offers a range of products for specialised knee procedures. The JOURNEY II BCS Total Knee System was launched in the US in 2013. It is designed to restore the normal kinematic motion by replicating the anatomic shapes of a normal, healthy knee.

The LEGION/GENESIS® II Total Knee System is a comprehensive system designed to allow surgeons to address a wide range of knee procedures from primary to revision.

These systems also feature VERILAST Technology, our advanced bearing surface and also utilised VISIONAIRE Patient-Matched Instrumentation.

With VISIONAIRE Instrumentation, a patient’s MRI and X-rays are used to create customised cutting blocks that allow the surgeon to achieve optimal mechanical axis alignment of the new implant. In addition, VISIONAIRE also helps save time by reducing the number of steps and instruments needed in the operating room.

Leadership in India

The Emerging & International Markets have become an increasingly important opportunity for our products. The acquisition of India’s Sushrut-Adler, a leader in trauma products, greatly enhanced our portfolio for this fast growing segment.

Sushrut-Adler has a long and distinguished history, a reputation for quality products and a loyal customer base. Its trauma portfolio strongly complements our established positions in orthopaedic reconstruction and sports medicine in India. From our enhanced platform we can develop further products for the mid-tier in India and for export. We are delivering on our Strategic Priorities to build leadership positions in the Emerging & International Markets and to bring forward products for these countries.
Segment performance: Advanced Surgical Devices continued

Hip Implants
For Hip Implants, core systems include the ANTHOLOGY Hip System, SYNERGY Hip System, the SMF Short Modular Femoral Hip System, the R3 Acetabular System, the POLARCRYSTAL Dual Mobility Hip System and the SL-PLUS Hip Family System.

In 2013, we launched the SMF Monolithic Hip Stem which is intended to capitalise on the clinically proven flat taper cementless primary stem. The SMF Monolithic Stem family of products allows the surgeon to use the convenience of a one piece stem and the advantage of a short stem.

We also introduced the POLARSTEM HA Cementless Stem System in the US for state-of-the-art minimally invasive surgical techniques that preserve bone and soft tissue, with good functionality and reproducible results.

Trauma & Extremities
Our Trauma & Extremities franchise offers both internal and external devices, as well as other products used in the stabilisation of severe fractures and deformity correction procedures.

During 2013, the US business refined its commercial model to increase the focus and resources addressing the opportunities in the high-growth trauma and extremities markets.

For Trauma, the principal internal fixation products are the TRIGEN® family of IM nails (TRIGEN META-NAIL System, TRIGEN Humeral Nail System, TRIGEN SURESHOT® and TRIGEN INTERTAN®) and the PERI-LOC® Plating System. For extremities and limb restoration, the franchise offers the TAYLOR SPATIAL FRAME® Circular Fixation System as well as a range of plates, screws, arthroscopes, instrumentation, resection, and suture anchor products for foot, ankle, hand and wrist surgeons.

2013 saw the introduction of the MODULAR RAIL SYSTEM (MRS) which is designed to correct bone deformities, malunions, non-unions and limb length discrepancies. The MRS takes advantage of the body’s ability to grow new bone tissue.

In Extremities during 2013 we expanded our ALL28® Foot and Ankle portfolio to include ankle instability and Achilles tendon repair. Ankle instability builds upon our successful TWINFIX® titanium anchor technology in a new system specifically designed for foot & ankle surgeons. It allows the surgeon to re-attach or repair the anterior talofibular ligament (ATFL) to the fibula. The Achilles tendon repair solution uses our FOOTPRINT® Ultra PK Suture Anchor to address traumatic avulsion of the tendon. This technology allows for tension adjustment after anchor insertion up until the inserter is removed, as well as eliminating knot stack on the heel that may cause irritation to the patient post procedure.

Sports Medicine Joint Repair
The Sports Medicine Joint Repair franchise offers surgeons a broad array of instruments, technologies and implants necessary to perform minimally invasive surgery of the joints, including knee, hip and shoulder repair.

Significant launches during the year included the HEALICOIL, REGENESORB Biocomposite Suture Anchor, Active Heel Traction Boot and CLANCY® Depth Gauge.

The HEALICOIL Suture Anchor’s distinctive, open-architecture differs from solid-core implants by eliminating the material between anchor threads, allowing blood and bone marrow from the surrounding cancellous bone to enter the implant. Our proprietary REGENESORB Material is an advanced biocomposite.

Arthroscopic Enabling Technologies (‘AET’)
Our Arthroscopic Enabling Technologies franchise offers healthcare providers a variety of technologies such as fluid management equipment for surgical access, high definition cameras, digital image capture, scopes, light sources and monitors to assist with visualisation inside the joints; radio frequency (‘RF’) probes, electromechanical and mechanical blades, and hand instruments for removing damaged tissue.

Key AET products include DYONICS shaver blades, ACUFEX® handheld instruments, and a wide range of radio frequency probes. The DYONICS Platinum Series Shaver Blades are single-use blades that provide superior resection due to their unequalled sharpness and virtually eliminate clogging through their improved debris evacuation capabilities.

The new LED 3000 Light Source launched in 2013 is designed to optimise the HD visualisation experience by providing brilliant illumination through a compact and intuitive interface.

Other ASD
The Other ASD franchise includes smaller businesses such as Gynaecology.

The main Gynaecology product is the TRUCLEAR® System, a first-of-its-kind hysteroscopic morcellator that pairs continuous visualisation capabilities with minimally invasive tissue removal providing safe and efficient removal of endometrial polyps and submucosal fibroids. The business also sells a hysteroscopic fluid management system, which provides uterine distension and clear visualisation during hysteroscopic procedures.
Natural-motion Journey II BCS Total Knee System

JOURNEY II BCS sets a new standard in knee implant performance by restoring more normal motion. This is achieved through the reproduction of both the shapes of the joint’s hard surfaces and the normal force behaviour of the soft tissues, such as ligament and muscle firing patterns. As a result, the soft tissue’s re-adjustment to new shapes and forces after surgery is minimised, helping to return the patient’s stride to its natural rhythm.

This latest innovation is the result of intense research and design, and the development of new PHYSIOLOGICAL MATCHING Technology. Using our LifeMOD human simulation software, Smith & Nephew engineers were able to conduct proprietary analysis of the bone, ligament and muscle forces that impact the knee, and then account for those forces within the design of an implant that restores anatomic shapes and normal motion.

JOURNEY II BCS is made from Smith & Nephew’s VERILAST Technology. The combination of two wear reducing materials – proprietary OXINIUM alloy and a highly cross-linked plastic liner, VERILAST Technology generates a significant reduction in implant wear compared to traditional bearing couples on the market.
Market and competition

In 2013, weaker economic conditions worldwide continued to create several challenges for the overall surgical devices market, including continued deferrals of joint replacement procedures and heightened pricing pressures. These factors contributed to the lower overall growth of the worldwide surgical devices market versus historic comparables. However, over the medium term, several catalysts are expected to continue to drive sustainable growth in surgical device procedures, including the growing and ageing population with active lifestyles, rising rates of co-morbidities such as obesity and diabetes, patient desire for minimally invasive procedures, technology improvements allowing surgeons to treat younger, more active patients, and the increasing demand for healthcare in emerging markets.

Orthopaedic and sports medicine procedures tend to be higher in the winter months (quarter one and quarter four in the US and Europe) when accidents and sports related injuries are highest. Conversely, elective procedures tend to slow down in the summer months due to holidays.

Global orthopaedic reconstruction segment

Smith & Nephew estimates that the global orthopaedic reconstruction segment is worth approximately $14 billion and the segment served by Smith & Nephew increased by approximately 3% in 2013. Competitors in the orthopaedic reconstruction segment include Biomet, DePuy Synthes (a division of Johnson & Johnson), Stryker and Zimmer.

Global orthopaedic trauma segment

Smith & Nephew estimates that the global orthopaedic trauma segment is worth approximately $5 billion and the segment served by Smith & Nephew grew by approximately 7% in 2013. Competitors in the orthopaedic trauma segment include Biomet, DePuy Synthes (a division of Johnson & Johnson), Stryker and Zimmer.

Global sports medicine segment

Smith & Nephew estimates that the global sports medicine segment (representing access, resection and repair products) is worth approximately $4 billion and the segment served by Smith & Nephew grew by approximately 6% in 2013. Competitors in the sports medicine segment include Arthrex, DePuy Mitek (a division of Johnson & Johnson) and Stryker.

Regulatory approvals

In 2013, regulatory clearances/approvals were obtained for several key products and instrumentations.

In the US, 510(k) clearance was obtained for Disposable Knee Instruments, SURESHOT Distal Targeting System v3.0 (added drill depth measurement functionality), HEALICOIL REGENESORB Suture Anchor, TWINFIX Ti 3.5mm SL Anchor, FOOTPRINT Ultra 4.5mm & 5.5mm SL Anchors, SUTUREFIX Ultra Suture Anchors and ULTRATAPE Suture.

In Europe, we obtained renewals for LEGION Narrow Femoral Components (CE mark approval), ULTRA FAST-FIX AB (indications expansion to include meniscal allograft transplantation), Round ENDOBUTTON, SCREWBUTTON and ULTRA FAST-FIX AB (CE Renewal).

In Canada, the TWINFIX Ti 3.5mm SL Anchor and FOOTPRINT Ultra 4.5mm & 5.5mm SL Anchors were approved.

In Australia, the OSTEORAPTOR Curved 2.3 system was approved.

In Japan, we received approvals for SURESHOT Distal Targeting System (two approvals obtained in 2013, including approval of current software version, 3.0), JOURNEY II BCS Knee System, R3 Acetabular System (XPE Liners and Shells), JOURNEY Uni Knee System (OXINIUM femoral components and all-poly tibial baseplates), JOURNEY Uni Knee System (Articular inserts and tibial baseplates), VISIONAIRE Patient-Matched Cutting Blocks, JOURNEY II CR Knee System, XTENDOBUTTON, HEALICOIL PK Suture Anchor, Beaver Blade, TRUCLEAR Hysteroscopic Morcellator system, BIOSURE HA Interference Screw, BIORAPTOR Knotless Anchor and TWINFIX ULTRA HA Suture Anchor.

In our Emerging & International Markets, we obtained a number of regulatory clearances/approvals for several core product lines, as follows:

In China, we received approvals for Ultra FASTFIX and Ultra FASTFIX AB Meniscal Repair System, SURESHOT Distal Targeting Systems, TWINFIX ULTRA HA Suture Anchor, SPYROMITE and DYNOMITE Extremities Suture Anchors and LEGION Primary Knee System – POROUS Femoral Component with HA Coating.

In Russia, we obtained approval to market our Multiple Knee Systems including JOURNEY UNI, GENESIS II, LEGION and TC_PLUS.

In Mexico, the OXINIUM Femoral Components, R3 Acetabular System, REDAPT Instruments, Cannulated Screw Systems were approved for distribution.
Segment performance: Advanced Wound Management

Advanced Wound Management

**REVENUE**
- **Advanced Wound Care**: 63%
- **Advanced Wound Devices**: 16%
- **Advanced Wound Bioactives**: 21%
- **Total**: $1,336m

**TRADING PROFIT**
- **Advanced Wound Care**: $237m
- **Advanced Wound Devices**: $247m
- **Advanced Wound Bioactives**: $233m
- **Total**: $275m

**OPERATING PROFIT**
- **Advanced Wound Care**: $213m
- **Advanced Wound Devices**: $144m
- **Advanced Wound Bioactives**: $180m
- **Total**: $190m

**TRADING PROFIT MARGIN**
- **Advanced Wound Care**: 20.6%
- **Advanced Wound Devices**: 12.6%
- **Advanced Wound Bioactives**: 9.7%

**FRANCHISE AREAS**
- Advanced Wound Care
- Advanced Wound Devices
- Advanced Wound Bioactives

**MANUFACTURING SITES**
- US and Canada: Oklahoma City OK and Calgary – Canada
- UK: Hull, Gilberdyke
- China: Suzhou
- Other: Curacao

**SERVICE CENTRES**
- US, UK, Germany, Japan and Australia

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1. The underlying percentage increases/decreases are after adjusting for the effect of currency translation and the inclusion of the comparative impact of acquisitions and exclusion of disposals.
2. Explanation of these non-GAAP financial measures are provided on pages 161 to 163.
Overview
In Advanced Wound Management (AWM) we offer products from initial wound bed preparation through to full wound closure. These products are targeted at chronic wounds associated with the older population, such as pressure sores and venous leg ulcers. There are also products for the treatment of acute wounds such as burns and invasive surgery that impact the wider population.

The main products within the AWM business are for Exudate management, Infection management, NPWT and Bioactives.

AWM has its global headquarters in Hull, UK and its North American headquarters in St Petersburg, Florida.

Advanced Wound Care

Exudate management
Exudate management products focus on effectively and efficiently locking away wound fluid and creating an optimal healing environment to ensure better healing outcomes. Our key brands in this space are ALLEVYN foam dressings and DURAFIBER gelling fibre dressings.

During 2013, we continued to invest in the commercialisation of ALLEVYN Life, our latest innovation in foam dressings, designed to provide a better quality of life to the patient during the healing process. In several studies this has resulted in better patient satisfaction, longer wear times and overall reduced healthcare management costs. One recent article published in the Journal of Community Nursing stated “In employing a design intended to combat the common problems of living with a wound, such as exudate leakage and conformability, the dressing has the potential to improve wound management practice and reduce the use of associated resources, such as nursing time”. The article concluded that around 2,500 working days could be saved annually as a result of using ALLEVYN Life.

DURAFIBER has continued to grow over the course of 2013, with customers switching from other products within the gelling fibre segment.

Infection management
AWM has two significant technologies in its infection management portfolio, silver (ACTICOAT, DURAFIBER Ag and ALLEVYN Ag) and iodine (IODOSORB®). The iodine-based IODOSORB® product has continued to gain interest as biofilms become a more important topic in wound care.

We launched DURAFIBER Ag in 2013 and with it entered the silver gelling fibre market, one of the largest segments of the infection management market.

Expanding Suzhou

In April distinguished guests from Suzhou Industrial Park and Jiangsu Province attended the official opening of the major extension to Smith & Nephew’s Advanced Wound Management manufacturing facility in Suzhou, China.

The expansion more than doubled the size of the Suzhou facility, and is enabling Smith & Nephew to continue to develop its product portfolio both for the Chinese market and for export. Those manufactured at Suzhou include ALLEVYN, Smith & Nephew’s leading foam dressing brand, which is used in the treatment of hard to heal wounds such as leg ulcers, as well as new portfolios for the mid-tier across the Emerging & International Markets.

Completed on time, to budget, and without a lost-time incident, the extension takes the total floor area to 27,000 square meters and doubles the production capacity to over 100 million wound dressings a year. We are delivering on our Strategic Priority to Simplify and Improve our Operating Model by optimising our global manufacturing footprint.

China is of great strategic importance to Smith & Nephew. We are proud of what we have achieved here and are investing for the long term. We now have more than 900 people in China, working across manufacturing and commercial operations. We have built our success upon a sustainable and ethical approach to business, and are bringing this long-term commitment to our work, our employees and our communities.
Other
We also offer a wide range of other wound care products, which means we have one of the most comprehensive ranges of wound care solutions in the industry. These products include our film and post-operative dressings, skincare products and gels.

ADERMA: Following the acquisition and integration of ADERMA pressure relieving technology in 2012, the launch in the UK and increase in ADERMA sales activity has seen it firmly established as the market leader. The UK government’s targeting of Pressure Ulcer Prevention and the known cost to the UK health system has driven the adoption of ADERMA in both the Acute and Community sectors. Due to the success in the UK, plans are in place to launch ADERMA as Dermapad in 2014 into other healthcare markets with equally strong Pressure Ulcer Prevention drivers. With our Skincare portfolio, ADERMA/Dermapad and ALLEYVN Life, we are well placed to deliver a strong and comprehensive Pressure Ulcer Prevention and treatment solution through a tested and validated value proposition into the Established Markets.

IV 3000: AWM’s specialist breathable premium IV dressing, utilising REALTIC® film technology and unique patterned adhesive, continues to perform well, particularly driven by emerging markets. Success in these markets and elsewhere has identified an opportunity for a mid-tier offering.

OPSITE POST OP VISIBLE: This is our innovative dressing that combines the qualities of a premium dressing with the ability to see the incision. This unique product continues to deliver strong growth in both our Established and Emerging & International Markets as its adoption becomes more widespread backed by good clinical evidence.

Advanced Wound Devices
Advanced Wound Devices consists of two categories of products, NPWT and VERSAJET®.

NPWT
Our NPWT solutions include traditional NPWT products (RENASYS® products) and the single-use portfolio (PICO and KALYPTO® products).

In its sixth year on the market, our RENASYS traditional NPWT brand has seen continuous improvement and innovation. Product updates in 2013 enhanced both function and user experience with our RENASYS systems as a whole. The RENASYS product offering now includes multiple device options, a choice of foam or gauze dressings, along with a range of drains and specialty kits.

The PICO system, our single-use, canister-free solution is revolutionising NPWT. As familiar and easy to use as an advanced wound dressing, PICO provides an active intervention to help promote optimal healing for early discharge and enhanced outcomes in complex cases. PICO simplifies NPWT.

VERSAJET
The VERSAJET Hydrosurgery system is a mechanical debridement device used by surgeons to excise and evacuate non-viable tissue, bacteria and contaminants from wound, burns and soft tissue injuries.

Advanced Wound Bioactives
Bioactives represent the fastest growing category of chronic wound therapeutics. Our diversified biotherapeutic portfolio offers novel, cost-effective solutions for tissue repair and healing, addressing the full spectrum of hard-to-heal wounds.

Currently, our leading product is Collagenase SANTYL® Ointment, the only FDA-approved biologic enzymatic debriding agent for chronic dermal ulcers and severe burns. Other products include: REGRANEX® Gel, a FDA-approved platelet-derived growth factor; and the OASIS® family of naturally-derived, extracellular matrix replacement products indicated for the management of both chronic and traumatic wounds.

Additionally, the lead candidate in our bioactive pipeline is HP802-247, an investigational allogeneic living cell bioformulation containing keratinocytes and fibroblasts. HP802-247 is currently in Phase III for the treatment of venous leg ulcers following positive Phase IIb clinical trial results, which were recently published in The Lancet.
Market and competition

The AWM market is focused on the treatment of chronic wounds of the older population and other acute hard-to-heal wounds such as burns and certain surgical wounds and is therefore expected to benefit from demographic trends. Growth is driven by an ageing population and by a steady advance in technology and products that are more clinically efficient and cost-effective than their conventional counterparts. The market for advanced wound treatments is relatively unpenetrated and it is estimated that the potential market is significantly larger than the current market. Management believes that the market will continue the trend towards advanced wound products with their ability to accelerate healing rates, reduce hospital stay times and cut the cost of clinician and nursing time as well as aftercare in the home.

Smith & Nephew estimates that the global wound management segment is worth approximately $7 billion and the segment served by Smith & Nephew grew by 4% in 2013. Global competitors vary across the various product areas and include Coloplast, Convatec, Kinetic Concepts and Molnlycke.

The 2013 Global NPWT market was flat versus 2012. Price pressures continue to offset the increase in patient therapy volumes. Price pressures have increased in some key markets due to competition, competitive bidding and reimbursement changes. Market size is estimated to be $2 billion.

Due to the nature of its product range there is little seasonal impact on the Advanced Wound Management business.

Regulatory approvals

In 2013, regulatory clearance was obtained for ALLEVYN Life Heel in the EU, US and Australia. ELECT® Super absorber was also approved in Europe. The complete range of DURAFIBER Ag sized dressings was approved in Europe and the US.

ALLEVYN Ag Gentle and ALLEVYN Ag Gentle Border were both approved in Japan. ALLEVYN Gentle Border and ALLEVYN Gentle were approved for import into China.

PICO Single Use Negative Wound Therapy System was approved in Brazil, Russia, Mexico and Korea.

The next generation VERSAJET II system was approved in Japan, China as well as several other Emerging & International Markets.

The RENASYS® EZ PLUS pump and RENASYS Foam and Gauze dressing kits were approved in China.

RENASYS EZ MAX Negative Pressure Wound Therapy pump also received clearance in the US, EU and Australia.

RENASYS EZ PLUS and RENASYS GO were both certified as compliant with the third edition of IEC 60601 an important standard for the safety of electro-medical devices.

2 EMERGING & INTERNATIONAL MARKETS

Building our product portfolio and commercial platform

We are building strong businesses in the Emerging & International Markets by having close, direct relationships with our customers – and by developing product portfolios that meet the needs of patients in the economic mid-tier.

In 2013 we furthered this strategy. Our first mid-tier product, a low cost camera system, was launched. We also acquired a portfolio of orthopaedic trauma products in India. By developing and manufacturing in the Emerging & International Markets we are able to deliver both quality and value.

We also completed acquisitions of distributors in Turkey and Brazil. Both these markets are fast-growing and offer exciting opportunities. These are important investments which will create a significant platform from which we can grow.

Smith & Nephew is delivering on its strategic priority to build a sustainable business in the Emerging & International Markets.
Healthpoint Biotherapeutics, acquired in late 2012, exceeded our expectations in its first year as a Smith & Nephew business. With strong revenue growth of 47%, it met our Strategic Priority of ‘Supplementing our Organic Growth through Acquisitions’.

The acquisition marked Smith & Nephew’s entry into Bioactives, the fastest growing segment of advanced woundcare. It also gives us enhanced presence in the US, including access to new channels and capabilities.

During 2013, we delivered on our objective to integrate Healthpoint gradually into Smith & Nephew to maximise the respective strengths of both companies and to avoid disruption to our customers.

Healthpoint’s culture very much complemented our own, with a clear focus on innovation, customer needs and a commitment to a high level of compliance and ethics. The integration team sought to retain the best on both sides – continuing to nurture the entrepreneurial spirit of Healthpoint, whilst bringing the wider benefits of Smith & Nephew’s global organisation to that business. The process culminated with the rebranding of Healthpoint to Smith & Nephew Biotherapeutics in September.

Smith & Nephew now has leading brands and positions in all the important Advanced Wound Management segments of Exudate Management, Infection Management, Negative Pressure Wound Therapy and Bioactives.
Our sustainability strategy supports our five Strategic Priorities

Smith & Nephew promotes sustainability to its stakeholders through addressing economic, social and environmental considerations. In turn, its sustainability strategy is aligned with the strategic priorities.

**Sustainability strategy and targets**

Progress towards the 2015 targets has been indexed to the baseline year 2011.

**Target by 2015**

<table>
<thead>
<tr>
<th>Objective</th>
<th>Target</th>
<th>Progress</th>
<th>Note</th>
</tr>
</thead>
<tbody>
<tr>
<td>Reduce non-renewable energy use by 15%</td>
<td>-0.6%</td>
<td>Energy consumption is decreasing but not in line with expectations. This is largely influenced by higher energy use in China as we scale up for expansion. The increased production levels at our Suzhou, China plant have given rise to an underlying increase in Group energy usage of 2.6%.</td>
<td></td>
</tr>
<tr>
<td>Reduce CO₂ emissions by 15%</td>
<td>+0.8%</td>
<td>CO₂ emissions reflect different carbon footprints of energy production in different geographic locations. Increasing production capacity at the Suzhou plant has contributed to an underlying increase in the carbon emissions of 3.6%. The carbon footprint in China is roughly twice that of the UK.</td>
<td></td>
</tr>
<tr>
<td>Reduce water use by 15%</td>
<td>+11.9%</td>
<td>Water usage continues to rise as new facilities are commissioned and we make operational choices based on best environmental options. For example, as we have expanded at Suzhou we have chosen to use a cooling system based on evaporation to reduce energy consumption. Water consumption at Memphis and Suzhou account for 84% of our total water usage and when excluded the increase was 7.6%.</td>
<td></td>
</tr>
<tr>
<td>Reduce packaging materials by 15%</td>
<td>-21.7%</td>
<td>The landfill component of our total waste was reduced by 21.7%.</td>
<td></td>
</tr>
<tr>
<td>Increase % of total waste recycled by 15%</td>
<td>+21.2%</td>
<td>Recycling of wastes continues to rise as more opportunities are exploited. We are now reporting separately the waste that is diverted for energy recovery. (Excludes waste to energy)</td>
<td></td>
</tr>
</tbody>
</table>

**ESTABLISHED MARKETS**

Making best environmental choices and manufacturing and supply chain efficiencies all contribute to reducing our cost base, facilitating access to our products and helping our customers meet their sustainability ambitions.

**EMERGING & INTERNATIONAL MARKETS**

Cost base reductions facilitate wider access to our products. Specifically our focus on mid-tier products is aimed at supporting fundamental and affordable healthcare in the Emerging & International Markets.

**INNOVATE FOR VALUE**

Building sustainability into our New Product Development processes, including reducing packaging and waste, helps us innovate to meet our customers’ expectations, deliver mutual value and optimise patient care.

**SIMPLIFY AND IMPROVE OUR OPERATING MODEL**

Incorporating sustainability into our business processes and optimising our facilities and supply chain to reduce our resource consumption and environmental impact help meet the expectations of our customers and society. Protecting our employees through the implementation of global HSE standards and responsible behaviours is not only right but also adds value to our business.

**SUPPLEMENT ORGANIC GROWTH WITH ACQUISITIONS**

Our due diligence approach includes sustainability considerations, our global policies and standards to ensure we protect the integrity and reputation of our business. Specifically our acquisition of Sushrut-Adler in India is aimed at providing fundamental and affordable healthcare into the emerging markets.
During the year, we have continued to make progress in reducing our energy consumption at many of our operational facilities. CO₂ emissions have not reduced in line with energy due to the different carbon footprints of energy production in different geographic locations, particularly China.

### Global GHG emissions data for current reporting year and comparisons

<table>
<thead>
<tr>
<th></th>
<th>2013</th>
<th>2012</th>
<th>2011</th>
</tr>
</thead>
<tbody>
<tr>
<td>Combustion of fuel and operation of facilities (process and fugitive)</td>
<td>10,102</td>
<td>10,922</td>
<td>10,894</td>
</tr>
<tr>
<td>Purchased electricity, heat and steam</td>
<td>66,659</td>
<td>64,991</td>
<td>65,241</td>
</tr>
<tr>
<td>Total</td>
<td>76,761</td>
<td>75,913</td>
<td>76,135</td>
</tr>
</tbody>
</table>

**Intensity Ratio**

<table>
<thead>
<tr>
<th>Emissions (total) normalised to:</th>
<th>2013</th>
<th>2012</th>
<th>2011</th>
</tr>
</thead>
<tbody>
<tr>
<td>CO₂e (t) per $m revenue (i)</td>
<td>18.9</td>
<td>18.3</td>
<td>17.8</td>
</tr>
<tr>
<td>CO₂e (t) per full-time employee (ii)</td>
<td>7.3</td>
<td>7.2</td>
<td>7.1</td>
</tr>
</tbody>
</table>

Notes

- 2013 data adjusted to exclude Healthpoint.
- Revenue data: 2013: $4,071m, 2012: $4,137m, 2011: $4,270m.

Support for community

In 2013, Smith & Nephew’s support for community charitable causes, grants, sponsorships and third party medical education was $10m.

For more information on sustainability see our website www.smith-nephew.com/sustainability

Our 2013 Sustainability Report will be published in spring 2014.

References

- Emission factors have been taken from the following source:

Safety performance

<table>
<thead>
<tr>
<th>Safety Reporting</th>
<th>2013</th>
<th>2012</th>
<th>2011</th>
</tr>
</thead>
<tbody>
<tr>
<td>OSHA recordable incidents per 200,000hrs worked (TIR)</td>
<td>1.11</td>
<td>1.09</td>
<td>1.16</td>
</tr>
<tr>
<td>Lost time incidents per 200,000hrs worked (LTIR)</td>
<td>0.48</td>
<td>0.51</td>
<td>0.58</td>
</tr>
<tr>
<td>Number of lost time incidents arising from manufacturing facilities</td>
<td>25</td>
<td>37</td>
<td>42</td>
</tr>
</tbody>
</table>

There were no fatalities. Lost time injuries in our manufacturing facilities decreased by 32% over the previous year. However, the number of injuries in our non-manufacturing and supply chain operations increased mainly due to car accidents. Improving driving safety is a particular priority in 2014. We are making significant progress with the deployment of risk based control processes and our new HSE Integrated Management System.

Greenhouse gases

Methodology, materiality and scope

We are reporting on the emission sources required under the Companies Act 2006 (Strategic Report and Directors’ Report) Regulations 2013. These sources fall within our consolidated financial statement. We have used the Greenhouse Gas Protocol: A Corporate Accounting and Reporting Standard (Revised Edition) as guidance for this process.

The focus of our data collection has been on the areas of the business that have the most influence on our environmental impacts and provide stakeholders with a level of detail that enables them to monitor emissions data, sustainability management and trends. Wherever possible, primary data from energy suppliers has been used.

The largest proportion of our environmental impacts is from manufacturing, warehousing and research. Sales locations are included however some smaller, leased or shared offices are not reported. We estimate that these exclusions represent less than 2% of our overall emissions.

The Biotherapeutics business (acquired at the end of 2012) is excluded from these figures along with other more recent acquisitions during 2013. This is in line with our established policy for integration of acquired assets.

Our emissions have been calculated by using specific emissions factors for each country outside the US and regional factors within the US. We have used the US EPA ‘Emissions & Generation Resource Integrated Database’ (eGRID) for US regions and the UK Government DEFRA Conversion Factors for Greenhouse Gas Reporting for elsewhere. We believe that these factors are the most appropriate to use for our business and give more accurate conversion rates than the conversion factors we have used in previous Sustainability Reports. The emissions from 2011, our baseline year for the sustainability targets, have therefore been recalculated using consistent rates. Fugitive emissions are included from the manufacturing and research locations and arise from the losses of refrigerant gases.

References

Emission factors have been taken from the following source:

Judicious financial management has been and remains central to our success.

1 The underlying percentage increases/decreases are after adjusting for the effect of currency translation and the inclusion of the comparative impact of acquisitions and execution of disposals.

2 The 2012 revenue by franchise has been restated to 2013 product franchises.
Revenue by market

The underlying increase in each division’s revenues, by market, reconciles to reported growth, the most directly comparable financial measure calculated in accordance with IFRS, as follows:

<table>
<thead>
<tr>
<th>Division</th>
<th>2013 $m</th>
<th>2012 $m</th>
<th>Reported growth in revenue %</th>
<th>Constant currency exchange effect %</th>
<th>Acquisition/Disposal effect %</th>
<th>Underlying growth in revenue %</th>
</tr>
</thead>
<tbody>
<tr>
<td>Advanced Surgical Devices US</td>
<td>1,391</td>
<td>1,449</td>
<td>(4)</td>
<td></td>
<td>2</td>
<td>5</td>
</tr>
<tr>
<td>Other Established Markets</td>
<td>1,204</td>
<td>1,298</td>
<td>(7)</td>
<td>2</td>
<td>2</td>
<td>(3)</td>
</tr>
<tr>
<td>Established Markets</td>
<td>2,595</td>
<td>2,747</td>
<td>(6)</td>
<td>1</td>
<td>4</td>
<td>(1)</td>
</tr>
<tr>
<td>Emerging &amp; International Markets</td>
<td>420</td>
<td>361</td>
<td>16</td>
<td>2</td>
<td></td>
<td>18</td>
</tr>
<tr>
<td>Advanced Surgical Devices</td>
<td>3,015</td>
<td>3,108</td>
<td>(3)</td>
<td>1</td>
<td>3</td>
<td>1</td>
</tr>
</tbody>
</table>

Advanced Wound Management

<table>
<thead>
<tr>
<th>Division</th>
<th>2013 $m</th>
<th>2012 $m</th>
<th>Reported growth in revenue %</th>
<th>Constant currency exchange effect %</th>
<th>Acquisition/Disposal effect %</th>
<th>Underlying growth in revenue %</th>
</tr>
</thead>
<tbody>
<tr>
<td>US</td>
<td>471</td>
<td>202</td>
<td>133</td>
<td></td>
<td>(111)</td>
<td>22</td>
</tr>
<tr>
<td>Other Established Markets</td>
<td>722</td>
<td>705</td>
<td>3</td>
<td>1</td>
<td>(1)</td>
<td>3</td>
</tr>
<tr>
<td>Established Markets</td>
<td>1,193</td>
<td>907</td>
<td>32</td>
<td>1</td>
<td>(23)</td>
<td>10</td>
</tr>
<tr>
<td>Emerging &amp; International Markets</td>
<td>143</td>
<td>122</td>
<td>17</td>
<td>3</td>
<td></td>
<td>20</td>
</tr>
<tr>
<td>Advanced Wound Management</td>
<td>1,336</td>
<td>1,029</td>
<td>30</td>
<td>1</td>
<td>(20)</td>
<td>11</td>
</tr>
</tbody>
</table>

Advanced Surgical Devices

Revenue

ASD revenue decreased by $93m (-3% on a reported basis) from $3,108m in 2012 to $3,015m in 2013. The underlying increase of 1% is after adjusting for a net 3% adverse impact from the disposal of the Clinical Therapies business in 2012 and the acquisitions completed in quarter four 2013, and a 1% unfavourable foreign currency translation.

In the US, revenue decreased by $58m to $1,391m in 2013 from $1,449m in 2012 (-4% on a reported basis). The underlying increase of 1% is after adjusting 5% for the adverse impact of the Clinical Therapies disposal in 2012. In Other Established Markets, revenue was $1,204m in 2013, a decrease of $94m from $1,298m in 2012 (-7% on a reported basis). The underlying decrease was 3% after adjusting for the adverse impact of 2% on the Clinical Therapies disposal in 2012, and 2% from unfavourable foreign currency translation. Our Emerging & International Markets revenue increased by $59m to $420m in 2013 from $361m in 2012 (16% increase on a reported basis). The underlying increase was 18% after adjusting 2% for unfavourable foreign currency translation.

In the global Knee Implant franchise, revenue decreased by $9m from $874m in 2012 to $865m in 2013 (-1% on a reported basis), representing flat underlying revenue performance after 1% of unfavourable currency translation. Growth has been impacted by exposure to a weakening European market with conditions continuing to deteriorate in Germany, our largest European market, and our position in the product life cycle versus our peers. Growth improved in the second half of the year driven by sales of the Journey II BCS Knee System and benefits from the VERILAST bearing surface TV advertising campaign in the US.

Global revenue from the Hip Implant franchise decreased by $13m from $666m in 2012 to $653m in 2013 (-2% on a reported basis), which represented an underlying revenue decline of 1% after 1% unfavourable foreign currency translation. Continuing metal-on-metal headwinds have contributed to this decline.

Trauma & Extremities revenue increased by $12m from $474m in 2012 to $486m in 2013 (5% on a reported basis). This represents underlying revenue growth of 4% after 1% of unfavourable foreign currency translation. During 2013, benefits were seen from the additional extremities US sales representatives recruited earlier in the year.

Sports Medicine Joint Repair revenue increased by $22m from $474m in 2012 to $496m in 2013 (5% on reported basis), representing underlying revenue growth of 7% and 2% of unfavourable foreign currency translation. This reflects a strong contribution across all key joint types and geographies.

Global revenue from Arthroscopic Enabling technologies decreased by $17m from $458m in 2012 to $441m in 2013 (-4% on a reported basis). This decrease represents an underlying revenue decline of 2% and 2% of unfavourable foreign currency translation.

The revenue in the Other ASD franchise fell by $88m from $162m in 2012 to $74m in 2013 following the disposal of the Clinical Therapies business in 2012. Excluding the impact of this disposal, underlying revenue in the Other ASD franchise, which includes gynaecology, grew by 14% with the remaining Clinical Therapies geographies contributing $9m.
Financial review and principal risks continued

Trading and operating profit
Operating profit, the most directly comparable financial measure under IFRS, reconciles to trading profit as follows:

<table>
<thead>
<tr>
<th></th>
<th>2013 $m</th>
<th>2012 $m</th>
</tr>
</thead>
<tbody>
<tr>
<td>Operating profit</td>
<td>620</td>
<td>632</td>
</tr>
<tr>
<td>Acquisition related costs</td>
<td>7</td>
<td></td>
</tr>
<tr>
<td>Restructuring and rationalisation costs</td>
<td>44</td>
<td>57</td>
</tr>
<tr>
<td>Amortisation of acquisition intangibles and impairments</td>
<td>41</td>
<td>39</td>
</tr>
<tr>
<td>Trading profit</td>
<td>712</td>
<td>728</td>
</tr>
</tbody>
</table>

Trading profit margin increased from 23.4% to 23.6%. Trading profit decreased by $16m to $712m from $728m in 2012. This reflects the impact of the CT disposal in May 2012, the impact of the US medical device excise tax and the cost of planned investments in the Knee Implants and Trauma franchises and Emerging & International Markets offset by benefits from our structural efficiency programme.

Operating profit decreased by $12m from $632m in 2012 to $620m in 2013. This comprises the decrease in trading profit of $16m discussed above, an increase in acquisition related costs of $7m, an increase in amortisation of acquisition intangibles of $2m, partially offset by a decrease in restructuring and rationalisation costs of $13m.

Advanced Wound Management
Revenue
AWM revenue increased by $307m (30% on a reported basis), from $1,029m in 2012 to $1,336m in 2013. The underlying increase of 11% is after adjusting for an increase of 20% for the acquisitions completed in the year and a 1% unfavourable foreign currency translation.

In the US, revenue increased by $269m to $471m in 2013 from $202m in 2012 (133% on a reported basis). The underlying increase of 22% is after adjusting 11% for the impact of acquisitions. In Other Established Markets, revenue was $722m in 2013, an increase of $17m from $705m in 2012 (3% on a reported basis). The underlying revenue increase was also 3% with the 1% impact of acquisitions offset by 1% of unfavourable foreign currency translation. Our Emerging & International Markets revenue increased by $212m in 2012 (17% on a reported basis). The underlying increase was 20% after adjusting 3% for unfavourable foreign currency translation.

Advanced Wound Care revenue decreased by $6m (1% on a reported basis) from $849m in 2012 to $843m in 2013. The underlying growth of 1% is after adjusting for foreign currency translation. Conditions across many European markets remain challenging but the introduction of the ALLEVYN Life range continues to make good progress across Europe following product introductions and investment in marketing.

Advance Wound Devices revenue increased from $180m in 2012 to $213m in 2013, a reported increase of $33m and 18%. The underlying growth of 20% is after adjusting for unfavourable foreign currency translations of 2%. This growth was impacted by continued gain in market share in NPWT, and our recent expansion into the emerging markets.

Advanced Wound Bioactives revenue of $280m in 2013 (2012 – $nil) relates to Healthpoint acquired in December 2012. The underlying increase, adjusted to include the results of Healthpoint for the commensurate period in 2012, was 47%.

Trading and operating profit
Operating profit, the most directly comparable financial measure under IFRS, reconciles to trading profit as follows:

<table>
<thead>
<tr>
<th></th>
<th>2013 $m</th>
<th>2012 $m</th>
</tr>
</thead>
<tbody>
<tr>
<td>Operating profit</td>
<td>190</td>
<td>214</td>
</tr>
<tr>
<td>Acquisition related costs</td>
<td>24</td>
<td>11</td>
</tr>
<tr>
<td>Restructuring and rationalisation costs</td>
<td>14</td>
<td>8</td>
</tr>
<tr>
<td>Amortisation of acquisition intangibles and impairments</td>
<td>47</td>
<td>4</td>
</tr>
<tr>
<td>Trading profit</td>
<td>275</td>
<td>237</td>
</tr>
</tbody>
</table>

Trading profit margin decreased from 23.1% to 20.6%. Trading profit increased by $38m to $275m from $237m in 2012. The increase in the year is primarily attributable to the full year benefit of the Healthpoint acquisition and growth in the Emerging & International Markets, partially offset by additional investment in R&D and sales and marketing. The decrease in trading margin reflects these same investments, combined with price and mix changes at a gross margin level.

Operating profit decreased by $24m from $214m in 2012 to $190m in 2013. This comprises of the increase in trading profit of $38m discussed above, offset by an increase of $43m in amortisation of acquisition intangibles and an increase in acquisition related costs of $13m, both due to the Healthpoint acquisition which completed in December 2012, and an increase in restructuring and rationalisation costs of $6m.

Principal risks and risk management
As an integral part of planning and review Group, business area and functional management seek to identify the significant risks involved in the business, and to review the risk management action plans for those risks. The Group Risk Committee, which is comprised of the Chief Executive Officer and Senior Executives, meets twice a year to review the risks identified by the businesses and corporate functions and any risk management actions being taken. As appropriate, the Risk Committee may re-categorise risks or require further information on the risk management action plans. The Risk Committee reports to the Board on an annual basis detailing all principal risks. In addition, the Board considers risk as part of the development of strategy. Internal audit reviews and the Audit Committee reports on the effectiveness of the operation of the risk management process.

There are known and unknown risks and uncertainties relating to Smith & Nephew’s business. The following pages provide an overview of what the Board considers the most significant risks that could cause the Group’s business, financial position and results of operations to differ materially and adversely from expected and historical levels, and how these risks relate to the Group’s strategic priorities. In addition, other factors not listed here that Smith & Nephew cannot presently identify or does not believe to be equally significant, could also materially adversely affect Smith & Nephew’s business, financial position or results of operations.
Disruptive technologies

The medical devices industry has a rapid rate of new product introduction. The Group must be adept at monitoring the landscape for technological advances, make good investment/acquisition choices, have an efficient and valuable product pipeline and secure protection for its intellectual property.

<table>
<thead>
<tr>
<th>Specific risks we face</th>
<th>Risk management actions</th>
<th>Possible impacts</th>
</tr>
</thead>
<tbody>
<tr>
<td>- Competitors may introduce a disruptive technology, or obtain patents or other intellectual property rights, that affect the Group’s competitive position</td>
<td>- Processes focused on identifying new products and potential disruptive technologies (internal and external)</td>
<td>Loss of market share, profit and long-term growth.</td>
</tr>
<tr>
<td>- Claims by third parties regarding infringement of their intellectual property rights</td>
<td>- Increasing productivity, prioritisation and allocation of R&amp;D funds</td>
<td></td>
</tr>
<tr>
<td>- Lack of innovation due to low R&amp;D investment, R&amp;D skills gap or poor product development execution for Established and Emerging &amp; International Markets</td>
<td>- Increasing R&amp;D investment in order to enhance clinical capability, invest in biomaterials</td>
<td></td>
</tr>
<tr>
<td>- Failure to successfully commercialise a pipeline product, or failure to receive regulatory approval</td>
<td>- Strengthen intellectual property rights</td>
<td></td>
</tr>
<tr>
<td>- Ineffective acquisition due diligence, valuation, purchase terms or integration</td>
<td>- Support an emerging market portfolio</td>
<td></td>
</tr>
<tr>
<td></td>
<td>- Business development resources and processes and investments to augment the internal product development</td>
<td></td>
</tr>
<tr>
<td></td>
<td>- Increasing speed to market of new products.</td>
<td></td>
</tr>
</tbody>
</table>

Link to Strategic Priority

3 INNOVATE FOR VALUE

4 SIMPLIFY AND IMPROVE OUR OPERATING MODEL

5 SUPPLEMENT THE ORGANIC GROWTH THROUGH ACQUISITIONS
Country risk, pricing and reimbursement pressure

In most markets throughout the world, expenditure on medical devices is controlled to a large extent by governments, many of which are facing increasingly intense budgetary constraints. The Group is therefore largely dependent on governments providing increased funds commensurate with the increased demand arising from demographic trends. Reimbursement rates may be set in response to perceived economic value of the devices, based on clinical and other data relating to cost, patient outcomes and comparative effectiveness. Political upheaval in the countries where the Group operates or surrounding regions could adversely affect Group operations or turnover.

Group operations are affected by transactional exchange rate movements. The Group’s manufacturing cost base is situated in the US, UK, China and Switzerland and finished products are exported worldwide.

<table>
<thead>
<tr>
<th>Specific risks we face</th>
<th>Risk management actions</th>
<th>Possible impacts</th>
</tr>
</thead>
<tbody>
<tr>
<td>Reduced reimbursement levels and increasing pricing pressures</td>
<td>Develop innovative economic product and service solutions for both Established and Emerging &amp; International Markets</td>
<td>Loss of revenue, profit and cash flows.</td>
</tr>
<tr>
<td>Reduced demand for elective surgery</td>
<td>Incorporate health economic component into design and development of new products</td>
<td></td>
</tr>
<tr>
<td>Increased focus on health economics</td>
<td>Enhanced expertise supporting reimbursement strategy and guidance</td>
<td></td>
</tr>
<tr>
<td>Government policies favouring lower priced and locally sourced products</td>
<td>Optimise cost to serve to protect margins and liberate funds for investment</td>
<td></td>
</tr>
<tr>
<td>Political upheavals prevent selling of products, receiving remittances of profit from a member of the Group or future investments in that country</td>
<td>Streamline COGS, SKUs, and inventory management</td>
<td></td>
</tr>
<tr>
<td>The Group is exposed to fluctuations in exchange rates. If the manufacturing country currencies strengthen against the selling currencies, the trading margin may be affected</td>
<td>The Group may transact forward foreign currency commitments when firm purchase orders are placed to reduce exposure to currency fluctuations.</td>
<td></td>
</tr>
<tr>
<td>Economic downturn impacts demand and collections</td>
<td>Develop innovative economic product and service solutions for both Established and Emerging &amp; International Markets</td>
<td></td>
</tr>
<tr>
<td>Increased generic and low cost products could impact revenue and profits.</td>
<td>Incorporate health economic component into design and development of new products</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Enhanced expertise supporting reimbursement strategy and guidance</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Optimise cost to serve to protect margins and liberate funds for investment</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Streamline COGS, SKUs, and inventory management</td>
<td></td>
</tr>
<tr>
<td></td>
<td>The Group may transact forward foreign currency commitments when firm purchase orders are placed to reduce exposure to currency fluctuations.</td>
<td></td>
</tr>
</tbody>
</table>

Supply, system and site disruption

Unexpected events could disrupt the business by affecting either a key facility or system or a large number of employees. The business is also reliant on certain key suppliers of raw materials, components, finished products and packaging materials.

<table>
<thead>
<tr>
<th>Specific risks we face</th>
<th>Risk management actions</th>
<th>Possible impacts</th>
</tr>
</thead>
<tbody>
<tr>
<td>Catastrophe could render one of the Group’s production facilities out of action</td>
<td>Ensure crisis response/business continuity plans at major facilities and for key products and key suppliers</td>
<td>Loss of revenue, profit and cash flows.</td>
</tr>
<tr>
<td>A significant event could impact key leadership or a large number of employees</td>
<td>Audit programme for critical suppliers and second sources or increased inventories for critical components</td>
<td></td>
</tr>
<tr>
<td>Issues with a single source supplier of a key component and failure to secure critical supply</td>
<td>Implement enhanced travel security and protection programme</td>
<td></td>
</tr>
<tr>
<td>A severe IT fault or cyber crime could disable critical systems and cause loss of sensitive data</td>
<td>IT disaster and data recovery plans are in place and support overall business continuity plans</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Mobile device and cyber security protection plan implementation.</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Link to Strategic Priority</th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>1 ESTABLISHED MARKETS</td>
<td></td>
<td></td>
</tr>
<tr>
<td>2 EMERGING &amp; INTERNATIONAL MARKETS</td>
<td></td>
<td></td>
</tr>
<tr>
<td>3 INNOVATE FOR VALUE</td>
<td></td>
<td></td>
</tr>
<tr>
<td>4 SIMPLIFY AND IMPROVE OUR OPERATING MODEL</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Product safety, regulation, and litigation

National regulatory authorities 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 and may also inspect for compliance with appropriate standards, including those relating to Quality Management Systems ('QMS') or Good Manufacturing Practice ('GMP') regulations. Design or manufacturing defects in products could result in product recalls and liability claims and impact revenues, profits and reputation.

<table>
<thead>
<tr>
<th>Specific risks we face</th>
<th>Risk management actions</th>
<th>Possible impacts</th>
</tr>
</thead>
<tbody>
<tr>
<td>Defective products supplied to Smith &amp; Nephew or failure in design or manufacturing process</td>
<td>Standardise the Group's quality management and practice</td>
<td>Loss of revenue, profit and reduction in share price.</td>
</tr>
<tr>
<td>New technology, product or processes changed by Smith &amp; Nephew or supplier do not identify product deficiencies</td>
<td>Monitoring and auditing programmes to assure compliance</td>
<td>Negative impact on brand/reputation.</td>
</tr>
<tr>
<td>Failure to implement programmes and supporting resources to manage quality and regulatory compliance</td>
<td>Group-wide product complaint and registration systems</td>
<td></td>
</tr>
<tr>
<td>Failure to manage, process and analyse customer complaints and adverse event data.</td>
<td>Group-wide practices to drive design, and production line performance and dependability</td>
<td></td>
</tr>
<tr>
<td>- Design for manufacture in product development</td>
<td>Post launch review of product safety and complaint data.</td>
<td></td>
</tr>
<tr>
<td>- Standardise the Group's quality management and practice</td>
<td>- Monitoring and auditing programmes to assure compliance</td>
<td></td>
</tr>
<tr>
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<tr>
<td>- Design for manufacture in product development</td>
<td>- Post launch review of product safety and complaint data.</td>
<td></td>
</tr>
<tr>
<td>- Post launch review of product safety and complaint data.</td>
<td>- Independent reporting channels for employees and third parties to report concerns with confidentiality</td>
<td></td>
</tr>
<tr>
<td>- Independent reporting channels for employees and third parties to report concerns with confidentiality</td>
<td>- Due diligence reviews and integration plans required for acquisitions.</td>
<td></td>
</tr>
<tr>
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<td>- Additional controls for interactions with healthcare professionals and government officials and for distributors and agents</td>
<td></td>
</tr>
<tr>
<td>- Additional controls for interactions with healthcare professionals and government officials and for distributors and agents</td>
<td>- Strong Group oversight bodies with supporting global compliance resources</td>
<td>Loss of profit and reduction in share price. Negative impact on brand/reputation.</td>
</tr>
<tr>
<td>- Strong Group oversight bodies with supporting global compliance resources</td>
<td>- Code of Conduct/Global Policies and Procedures ('GPPs') providing controls for significant compliance risks</td>
<td></td>
</tr>
<tr>
<td>- Code of Conduct/Global Policies and Procedures ('GPPs') providing controls for significant compliance risks</td>
<td>- Training and e-resources to guide employees and third parties with compliance responsibilities</td>
<td></td>
</tr>
<tr>
<td>- Training and e-resources to guide employees and third parties with compliance responsibilities</td>
<td>- Monitoring and auditing programmes to verify implementation</td>
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<td></td>
</tr>
</tbody>
</table>

Compliance with laws and regulations

Business practices in the healthcare industry are subject to increasing scrutiny by government authorities. The trend in many countries is towards increased enforcement activity. The Group is also subject to increased regulation of personal information. Acquisitions and expansion into emerging markets could also require additional compliance resources.

<table>
<thead>
<tr>
<th>Specific risks we face</th>
<th>Risk management actions</th>
<th>Possible impacts</th>
</tr>
</thead>
<tbody>
<tr>
<td>Violation of healthcare, data privacy or anti-corruption laws could result in fines, loss of reimbursement and impact reputation</td>
<td>Strong Group oversight bodies with supporting global compliance resources</td>
<td>Loss of profit and reduction in share price. Negative impact on brand/reputation.</td>
</tr>
<tr>
<td>Serious breaches could potentially prevent the Group from doing business in a certain market</td>
<td>Code of Conduct/Global Policies and Procedures ('GPPs') providing controls for significant compliance risks</td>
<td></td>
</tr>
<tr>
<td>Failure to conduct adequate due diligence or to integrate appropriate internal controls into acquired businesses could result in fines and impact return on investment.</td>
<td>Training and e-resources to guide employees and third parties with compliance responsibilities</td>
<td></td>
</tr>
<tr>
<td>- Strong Group oversight bodies with supporting global compliance resources</td>
<td>- Monitoring and auditing programmes to verify implementation</td>
<td></td>
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<tr>
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</table>

By order of the Board, 26 February 2014

Susan Swabey
Company Secretary