SMITH & NEPHEW PLC
Form 20-F
March 05, 2018

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 20-F

(Mark One)

REGISTRATION STATEMENT PURSUANT TO SECTION 12(b) OR (g) OF THE SECURITIES EXCHANGE ACT OF 1934
or

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended December 31, 2017

or

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
or

SHELL COMPANY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
Commission file number 1-14978

Smith & Nephew plc

(Exact name of Registrant as specified in its charter)

England and Wales

(Jurisdiction of incorporation or organization)

15 Adam Street, London WC2N 6LA

(Address of principal executive offices)

Securities registered or to be registered pursuant to Section 12(b) of the Act:

Title of each class	Name on each exchange on which registered
American Depositary Shares	New York Stock Exchange
Ordinary Shares of 20¢ each	New York Stock Exchange*

*Not for trading, but only in connection with the registration of American Depositary Shares, pursuant to the requirements of the Securities and Exchange Commission.

Securities registered or to be registered pursuant to Section 12(g) of the Act: None.

Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act: None.

Indicate the number of outstanding shares of each of the issuer's class of capital or common stock as of the close of the period covered by the annual report: 890,855,310 Ordinary Shares of 20¢ each

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act Yes No

If this report is an annual or transition report, indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 Yes No

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days: Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required

to submit and post such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or an emerging growth company.

Large Accelerated Filer Accelerated Filer Non-accelerated filer
Emerging growth company
If an emerging growth company that prepares its financial statements in accordance with U.S. GAAP, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards† provided pursuant to Section 13(a) of the Exchange Act. Yes No

† The term "new or revised financial accounting standard" refers to any update issued by the Financial Accounting Standards Board to its Accounting Standards Codification after April 5, 2012.

Indicate by check mark which basis of accounting the registrant has used to prepare the financial statements included in this filing.

U.S. GAAP International Financial Reporting Standards as issued by the International Accounting Standards Board
Other
If "Other" has been checked in response to the previous question indicate by check mark which financial statement item the registrant has elected to follow: Item 17 Item 18

If this is an annual report, indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

Indicate by check mark whether the registrant has filed all documents and reports required to be filed by Sections 12, 13 or 15(d) of the Securities Exchange Act of 1934 subsequent to the distribution of securities under a plan confirmed by a court. Yes No

CONTENTS

Front cover: Employees from Smith & Nephew's Expert Connect Centre, Watford, UK – Natalia Zielinska (middle) Bioskills Laboratory Manager, Alejandra Alvarez Pineda (left) and Michael Mead, Bioskills Laboratory Specialists (right).

TRAINING & EDUCATION PAGE 32

We are a constituent of the UK's FTSE100 and our shares are traded on the London Stock Exchange and through American Depositary Receipts on the New York Stock Exchange (LSE: SN, NYSE: SNN).

The Strategic Report, which has been prepared in accordance with the requirements of the Companies Act 2006, comprises the first five sections above and has been approved and signed on behalf of the Board. The Directors' Report comprises pages 6, 16–17, 25–28, 33–39, 42–78, 107, 140-142, 158 and pages 171–193 of the Annual Report.

Smith & Nephew is a global medical technology business that has been supporting healthcare professionals to improve patients' lives since 1856.

DRIVING PERFORMANCE

PIONEERING INNOVATION

& ENSURING TRUST

We do this by taking a pioneering approach to the design of our advanced medical products and services, by securing wider access to our diverse technologies for more customers globally, and by enabling better outcomes for patients and healthcare systems.

We have leadership positions in:

Orthopaedic Reconstruction and Trauma

Joint replacement systems for knees and hips and products to help repair broken bones

Advanced Wound Management

Treatment and prevention products for hard-to-heal wounds

Sports Medicine

Implants and enabling technologies for minimally invasive repair of the joint

FIND MORE ONLINE

To learn more about Smith & Nephew,

to register to receive our news,

or to explore opportunities to join us,

please visit www.smith-nephew.com

CHAIRMAN'S STATEMENT

PROVIDING

LEADERSHIP

The Board approaches 2018 with optimism. Olivier has built a strong foundation and we expect to attract someone of the highest calibre to accelerate business performance from this base.

DEAR SHAREHOLDER

One of the core duties of a Board is to ensure that companies evolve to meet the ever changing challenges and opportunities they face. A Board must set the pace in this, refreshing and strengthening its membership with deeper expertise, new perspectives and greater diversity.

Since becoming Chairman in 2014 I am pleased with the evolutionary changes we have made at Smith & Nephew. I believe these build on the successes of the past and position the Company well for further progress.

STRENGTHENING THE BOARD

We have been able to attract new Non-Executive Directors of high calibre to replace Board members retiring after completing their service.

Angie Risley, who joined in September 2017, is currently Group HR Director of J Sainsbury plc and was previously Non-Executive Director of Arriva plc, Biffa plc and Serco plc where she was also chairman of the Remuneration Committee. Marc Owen, recently retired from the Executive Committee of Fortune 500 healthcare business McKesson Corp, where he was Chairman of Celesio AG and President of McKesson Speciality Health, and previously a healthcare and technology specialist at McKinsey, joined in October 2017. Roland Diggelmann, Chief Executive Officer at Roche Diagnostics and a member of the Corporate Executive Committee of F. Hoffmann-La Roche Ltd, and previously a senior executive at Zimmer GmbH, will join on 1 March 2018.

Marc and Roland strengthen the Board's knowledge of commercial healthcare and the medical devices sector while Angie will provide effective leadership to our Remuneration Committee when Joe Papa steps down at the AGM in April. Joe has been a highly valued colleague and exemplary steward of Smith & Nephew. On behalf of the whole Board, I thank him for his service.

CHIEF EXECUTIVE OFFICER

In October Olivier Bohuon notified the Board of his intention to retire by the end of 2018, after seven years as Chief Executive Officer. Under Olivier's leadership Smith & Nephew has undergone important and necessary change and he has significantly strengthened the foundations of our Company. As Smith & Nephew enters its next chapter, the Board is determined to build on this.

Olivier continues to lead Smith & Nephew and drive the Company's growth initiatives and operating plans. In this he is supported by our new Chief Financial Officer, Graham Baker, who joined in March 2017.

The Board has been impressed with Graham's strong start as he quickly developed his understanding of the business and we welcome his commercial acumen and attention to detail. Our views of Graham have been echoed by the positive shareholder feedback we have received.

GOVERNANCE AND CULTURE

In 2017 the Board invested significant time meeting local management and employees and understanding market dynamics. These included visiting our offices in Dubai, Tokyo and Hull, as well as some Board members spending time with our salesforce to better appreciate their role and meeting customers. In addition to giving us commercial insight, such activities let us get anecdotal evidence of the culture at Smith & Nephew, something the Board puts great value on. We strive to set the tone from the top, and review data to demonstrate performance, but it is only by meeting employees from all levels of the Company that we can be certain that Smith & Nephew's values of I perform, I innovate and I earn trust are being lived across the business.

We conducted our regular review of strategy and Group structure at our annual strategy meeting in October, ensuring the continued close alignment of Board and management on our expectations and current direction. We upgraded our Risk Management process and strengthened our internal team in this area. Our Senior Independent Director, Ian Barlow, conducted a Board Effectiveness Review which identified some areas of further improvement which we are focusing on, such as deepening our knowledge of the competitive landscape to enable us to better support management develop and deploy resources to win in our chosen markets. I encourage you to read more about these and other matters in our Governance section starting on page 50.

2017 PERFORMANCE

The Board receives regular updates on the performance of the business from the CEO and CFO, together with members of the senior management team attending Board meetings over the course of the year.

We could clearly see areas of the business where the Company excelled in 2017, such as Global Operations where we have improved quality and supply, and R&D, where we have an exciting new product pipeline. It is no coincidence that both of these areas of the business have effective leaders who impressed the Board during 2017.

Whilst the trading performance of the Group was better than in 2016, and we delivered within our guidance, we continue to endorse the Chief Executive's view that this business can and should deliver better results and reinforce the need for continued focus on driving better execution.

The 2017 full year dividend of 35.0¢ per share reflects the strong growth in adjusted earnings per share.

The Board approaches 2018 with optimism. Olivier has built a strong foundation and we expect to attract someone of the highest calibre to accelerate business performance from this base. Thank you for your support and engagement in 2017 and the Board looks forward to serving you into an exciting next chapter for Smith & Nephew.

Yours sincerely,

Roberto Quarta

Chairman

FINANCIAL HIGHLIGHTS

$4,765m	+2%	+3%		35.0¢	+14%
Revenue	Reported	Underlying1		Dividend per share	
Group revenue was up 2% on a reported basis (including -1% headwind from the 2016 Gynaecology business disposal) and 3% on an underlying basis, in line with guidance.				The 14% year-on-year increase reflects the strong growth in adjusted earnings per share.	
$934m	+17%	$1,048m	+3%	87.8¢	
Operating profit		Trading profit1		Earnings per share (EPS)	
Operating profit margin of 19.6% is up 240bps year-on-year due to more favourable non-trading items.		Trading profit margin1 was 22.0%, up 20bps year on year, in line with guidance.		In 2016 EPS benefited from the gain on the disposal of the Gynaecology business.	
94.5¢	+14%	14.3%	+280bps	5%	
Adjusted Earnings per share1 (EPSA)		Return on Invested Capital1 (ROIC)		R&D expenditure	
Reflects one-off tax benefits, improvements in trading profit margin and the tax rate on trading1.		Reflects improvements in operating profit, the lower tax rate and a stable asset base.		To drive innovation, we maintain our investment in R&D at around 5% of Group revenue.	

1 These non-IFRS financial measures are explained and reconciled to the most directly comparable financial measure prepared in accordance with IFRS on pages 178–181.

FINANCIAL REVIEW PAGE 36 OUR BOARD OF DIRECTORS PAGE 50 GOVERNANCE PAGE 56

CHIEF EXECUTIVE OFFICER'S REVIEW

STRONGER

SMITH & NEPHEW

In 2018, I expect Smith & Nephew to build on 2017 by delivering another year of improved performance driven by our strong product portfolio and pipeline of innovative products.

DEAR SHAREHOLDER

We delivered on our promises to improve the top and bottom line in 2017. Our healthy balance sheet, good cash generation and increased dividend demonstrate the robust foundations underpinning our business. In 2018, I expect Smith & Nephew to build on 2017 by delivering another year of improved performance driven by our strong product portfolio and pipeline of innovative products.

STRATEGIC PRIORITIES

In my first year as Chief Executive, in 2011, we set five strategic priorities that have shaped a fundamental management and operational restructuring of the Group as a foundation to improving its growth and profit profile. Through these priorities we continue to drive our business forward.

In 2017 I was pleased with the resultant commercial performance in many areas. In Knee Implants we had an outstanding year, Trauma and Extremities and Advanced Wound Devices also, and we returned the Emerging Markets to double-digit revenue growth.

Of course, there are some areas that did not meet my expectations, such as in Arthroscopic Enabling Technologies and European Wound Care. These are not because of new issues, but they are taking longer to improve than expected. We are attacking the underlying issues with renewed vigour in 2018.

You can read more about our performance against each of the strategic priorities in the next few pages (pages 10–15). I would like to draw your attention to how our strong new product portfolio reflects our decision of a few years ago to increase our investment in disruptive R&D and technology acquisitions.

One of our best recent achievements was to create a global R&D organisation that became fully operational in 2017 and is building on these successes. We now have greater visibility across our development portfolio to ensure we back the winners of the future in areas such as digital, robotics and biologics. We are making better decisions and hitting milestones consistently, and this will underpin our success for many years to come.

ACCELERATING PERFORMANCE & INNOVATION

As we have transformed Smith & Nephew, so our markets and industry have changed. We are seeing an increasingly competitive environment: new selling models, new entrants, pricing pressure and increasing costs – which in some markets are outpacing our growth. We also see great opportunity to invest behind pioneering technologies which take market share, offer a wider selection of commercial terms to suit more customers, expand our reach in the emerging markets and start to realise the benefits of the digital revolution for our industry.

In late 2017 we undertook a review of our business to look for opportunities to achieve higher growth targets, strengthen our competitive position, and make us more agile to changes in the market. As a result, in early 2018 we introduced the APEX programme, which stands for ‘Accelerating Performance and Execution’. APEX will make key enhancements to our business and ways of working over the next five years. We expect this programme to deliver $160 million of annualised benefits by 2022. APEX is now possible because of the work put in to create our strong Group structure, and it will build on this robust base. More information on APEX can be found on page 14.

BUILDING A WINNING CULTURE

Our success as a Company is made possible by talented employees working together for our shared mission: to support healthcare professionals in their efforts to improve patients’ lives. This is why being a great place to work is important to us, and why every two years we measure our progress toward this goal with our Global Employee Survey.

Our survey tool is the Great Place to Work Institute’s Trust Index, and in 2017 we performed strongly across the dimensions of vision, recognition, pride and equality. We now have nine countries accredited as a Great Place to Work.

We put great store by our culture, and work to embrace diversity, encourage progression, and reward success. We also want our employees to put something back into their communities. Our People section on pages 25–28 describes our commitments and actions across all of these areas.

LOOKING TO THE FUTURE

In October 2017 I announced my decision to retire from Smith & Nephew by the end of 2018. As I looked ahead to the next long-term phase of growth, I decided that it was the right time to announce my retirement plans, providing ample time to identify a successor and ensure a smooth transition.

In the meantime, I remain resolutely focused on delivering our commitments for 2018, while positioning the Company for further success. Looking further ahead, our greater focus on commercial execution gives us confidence we will

outgrow our markets and the new APEX programme supports our expectation of improved trading profit margin.

Yours sincerely,

Olivier Bohuon

Chief Executive Officer

OUR STRATEGIC PRIORITIES

Our strategic priorities guide our actions to support healthcare professionals and transform our growth profile.

WHO WE ARE

ONE GLOBAL BUSINESS

WITH MORE THAN 15,000 EMPLOYEES

OUR VALUES AND HOW WE ACT

Our values shape everything that we do as a business and form the basis of our relationships with all our stakeholders.

Performance

Performance means being responsive to the needs of our customers and their patients, setting ourselves clear goals and standards and achieving them.

Innovation

Innovation means being energetic, creative and passionate about everything we do, anticipating customers' needs and overcoming barriers and developing opportunities.

Trust

Trust is something we understand that we have to earn and we strive to operate with integrity and take an ethical approach to business.

AN INTEGRATED BUSINESS

UNITED STATES (US)

The United States is the Group's largest market representing 48% of our global revenue. Due to its commercial importance to the Group, its revenue is reported separately. The United States is also home to a number of our manufacturing facilities.

OTHER ESTABLISHED MARKETS

Other Established Markets comprise commercial operations in Europe, Australia, Japan, Canada, and New Zealand, We have manufacturing facilities in the UK, Germany and Switzerland.

EMERGING MARKETS

Emerging Markets include our commercial businesses in China, Asia, India, Russia, Middle East, Africa and Latin America.

These generated 16% of Group revenue in 2017. We have manufacturing facilities in China, Costa

		Rica, India, Russia and Curacao.
2017 revenue	2017 revenue	2017 revenue
$2,306m	$1,678m	$781m
0% +2%	0% 0%	+13% +12%
Reported Underlaying1	Reported Underlaying1	Reported Underlaying1
	ORTHOPAEDIC RECONSTRUCTION AND TRAUMA	
	SPORTS MEDICINE	
	ADVANCED WOUND MANAGEMENT	
	GLOBAL FUNCTIONS2	

1 These non-IFRS financial measures are explained and reconciled to the most directly comparable financial measure prepared in accordance with IFRS on pages 178–181.
2 Commercial Excellence including Global Marketing, R&D, Manufacturing & Supply Chain, Central Support.

SMITH & NEPHEW ANNUAL REPORT 2017 OVERVIEW 7

SELLING NINE PRODUCT FRANCHISES

KNEE IMPLANTS	SPORTS MEDICINE JOINT REPAIR	ADVANCED WOUND CARE
HIP IMPLANTS	ARTHROSCOPIC ENABLING TECHNOLOGIES	ADVANCED WOUND BIOACTIVES
TRAUMA & EXTREMITIES	OTHER SURGICAL BUSINESSES	ADVANCED WOUND DEVICES

SUPPORTING HEALTHCARE PROFESSIONALS IN MORE THAN 100 COUNTRIES

Revenue by products			Revenue by geography	
A	KNEE IMPLANTS	$984m	A UNITED STATES	$2,306m
B	HIP IMPLANTS	$599m	B OTHER ESTABLISHED MARKETS	$1,678m
C	TRAUMA & EXTREMITIES	$495m	C EMERGING MARKETS	$781m
D	SPORTS MEDICINE JOINT REPAIR	$627m		
E	ARTHROSCOPIC ENABLING TECHNOLOGIES	$615m		
F	OTHER SURGICAL BUSINESSES	$189m		
G	ADVANCED WOUND CARE	$720m		
H		$342m		

	ADVANCED WOUND BIOACTIVES	
I	ADVANCED WOUND DEVICES	$194m

OUR BUSINESS MODEL

HOW WE
CREATE VALUE

THE RESOURCES WE NEED
OUR PEOPLE
Engaging, developing and retaining our more than 15,000 employees is important to us and we work hard to be a great place to work as well as a responsible corporate citizen.
RESEARCH & DEVELOPMENT
Innovation is part of our culture and we invest 5% of our revenue to develop new products that will help improve patients' lives.
MANUFACTURING & QUALITY
We operate our global manufacturing efficiently, and at the highest possible standards, to ensure product quality at competitive pricing.
SALES & MARKETING
We support our customers in over 100 countries. Our commercial teams are highly specialised with an in-depth knowledge across the full range of product franchises.
ETHICS & COMPLIANCE
We are committed to doing business the right way and apply strict business principles to the way we deal with our customers and partners.
TRAINING & EDUCATION
Every year, thousands of healthcare professionals attend our training courses around the world. Education is fundamental to how we support our customers.
THE RESOURCES WE NEED PAGE 25

A FOCUS ON

PERFORMANCE

OUR VALUE PROPOSITION
Our mission is to support healthcare professionals by providing advanced medical devices that they use in their daily efforts to improve the lives of their patients.
PIONEERING APPROACH

We take a pioneering approach to the design of our products and services. Smith & Nephew has a long history of innovation, dating back to our foundations in the 19th century, and today we support customers to manage and prevent disease states, and enable swifter recovery for their patients.

ENSURING WIDER ACCESS

We strive to secure wider access to our advanced technologies for more customers globally. In emerging markets we have built an entrepreneurial business resourced to reach and support an ever greater number of customers in delivering affordable healthcare.

ENABLING BETTER OUTCOMES

We seek to enable better outcomes for patients and healthcare systems, providing high quality products and appropriate training to improve clinical outcomes, enabling healthcare professionals to treat more patients and improving the economic outcome for payers.

CREATING

PRODUCTS

We have leadership positions in Orthopaedic Reconstruction and Trauma, Advanced Wound Management and Sports Medicine:
– Knee Implants
– Hip Implants
– Trauma & Extremities
– Sports Medicine Joint Repair
– Arthroscopic Enabling Technologies
– Other Surgical Businesses
– Advanced Wound Care
– Advanced Wound Bioactives
– Advanced Wound Devices

OUR PRODUCTS PAGE 18

FOR OUR

CUSTOMERS

We service our customers through our dedicated and highly trained global sales force and selected third party sellers:
– Surgeons
– Nurses
– Nurse specialists
– Physicians, GPs
– Healthcare systems
– Procurement groups
– Payers, administrators
– Retail, consumers, patients

THE OUTPUT OF WHAT WE DO

FINANCIAL PERFORMANCE

Targeting higher revenue growth and a better trading profit margin.

$4,765m
Revenue

$934m
Operating Profit

$1,048m
Trading Profit1

CAPITAL ALLOCATION FRAMEWORK

Prioritising the use of cash and ensuring an appropriate capital structure.

$269m
Dividend

IMPROVED QUALITY OF PATIENTS' LIVES

Providing our advanced medical devices in more than 100 countries.

100+
countries

TRAINING AND EDUCATION

Supporting HCPs and ensuring the safe and effective use of our products.

45,000+
surgeon training instances
GREAT PLACE TO WORK
Supporting and encouraging employees to live our values.
15,000+
employees
A SUSTAINABLE BUSINESS
Working in a sustainable, ethical and responsible manner everywhere we operate.
160+
years of proud history

1 These non-IFRS financial measures are explained and reconciled to the most directly comparable financial measure prepared in accordance with IFRS on pages 178–181.

STRATEGIC PRIORITIES

MAXIMISING OUR PERFORMANCE

Smith & Nephew has a clear vision to build a successful, sustainable business. This vision is encapsulated in our corporate value proposition – supporting healthcare professionals by taking a pioneering approach to the design of our advanced medical products and services, by securing wider access to our diverse technologies for more customers globally, and by enabling better outcomes for patients and healthcare systems.

We are focused on transforming the growth profile of the business while delivering this proposition. We are working to rebalance the Group towards higher growth opportunities. Over the last five years, Smith & Nephew has materially improved the mix of higher growth potential to lower growth businesses, shifting from one-third higher growth to over 50% today.

Our strategic priorities, introduced in 2011, guide our actions in delivering these twin aspirations of supporting healthcare professionals and transforming our growth profile.

OUR STRATEGIC PRIORITIES

BUILD A STRONG POSITION IN ESTABLISHED MARKETS

Build on existing strong positions, win market share through greater product and commercial innovation and drive efficiencies to liberate resources.

SEE OPPOSITE

FOCUS ON EMERGING MARKETS

Deliver leadership in the Emerging Markets by building strong, direct customer relationships, widening access to our premium products and developing portfolios designed for the economic mid-tier population.

PAGE 12

INNOVATE FOR VALUE

Deliver pioneering products and business models that improve clinical and health economic outcomes and widen access across geographies and patient groups.

PAGE 13

SIMPLIFY AND IMPROVE OUR OPERATING MODEL

Pursue maximum efficiency in everything we do, streamline our operations and manufacturing, remove duplication and build strong global functions to support our commercial teams.

PAGE 14

SUPPLEMENT ORGANIC GROWTH WITH ACQUISITIONS

Build our platform by acquiring complementary products or businesses in our higher growth segments and manufacturing and distribution capabilities in the Emerging Markets.

PAGE 15

BUILD A STRONG POSITION IN ESTABLISHED MARKETS

Established Markets for Smith & Nephew are the US, Europe, Australia, Japan, Canada and New Zealand. Smith & Nephew delivered 84% of its revenue from these countries in 2017.

In the United States, our single largest country representing 48% of global revenue, reported revenue growth was flat and underlying growth was 2%. The Other Established Markets growth rate was flat on both an underlying and reported basis.

In 2017 we focused on improving our commercial execution. With a simpler and more agile commercial structure in each country, supported by global functions, we sought to drive improved performance and greater efficiency. This was supported by sales force excellence initiatives including a sharper focus on both health economic and clinical evidence to support our products.

In Reconstruction, the Knee Implants franchise performed well, with the JOURNEY™ II Total Knee System driving good growth, as did the LEGION™ Revision Knee System. In Hip Implants, the new REDAPT™ Revision and POLARSTEM™ Cementless Stem systems were well received. In Trauma & Extremities, new clinical evidence supported increased uptake of our TRIGEN™ INTERTAN™ hip fracture system.

Sports Medicine Joint Repair performance was driven by good demand for our shoulder repair portfolio, and we added an exciting new technology when we acquired Rotation Medical (see page 15 for more). Arthroscopic Enabling Technologies was impacted by continued softness in mechanical resection. The roll-out of our LENS™ visualisation and WEREWOLF™ COBLATION™ systems are underway and we expect an increasing contribution from these in 2018.

In the US, and other countries, we are seeing a shift towards day-case surgery for total joints starting to take place in Ambulatory Surgery Centre (ASCs), something Smith & Nephew is uniquely positioned to benefit from. Through Sports Medicine we are already a partner to many ASCs. We believe we can leverage this customer knowledge and relationships to improve the performance of our knee implants franchise. Our portfolio is well-suited for ASCs where early mobility and efficiency are key, as is our robotic NAVIOTM Surgical System due to its small footprint, portability and cost.

The Advanced Wound Care franchise delivered strong growth in the US, but was held back by softer market conditions in Europe. In Advanced Wound Bioactives, SANTYL™ benefited from a new analysis demonstrating its effectiveness in advancing pressure ulcers through the healing process2, improving performance in the second half of the year. Advanced Wound Devices performed strongly across the year, led by the continued success of our single use negative pressure wound therapy (sNPWT) device PICO™.

$3,984m
Revenue from Established Markets

84%
of Group revenue
0% +1%
Reported Underlying1
WHY THIS KPI IS IMPORTANT

We use this KPI to track the relative strength of our position in these markets.

HOW WE PERFORMED

Growth in the US, our largest market, was offset somewhat by softer conditions in some other markets.

1 These non-IFRS financial measures are explained and reconciled to the most directly comparable financial measure prepared in accordance with IFRS on pages 38 and 178–181.

2 Advances in Wound Care. Gilligan, A.M., et al. Comparative effectiveness of Clostridial Collagenase Ointment to medicinal honey for treatment of pressure ulcers. Volume 6, Number 4 (April 2017).

SUPPORTING CUSTOMERS AT THE ECC

“It’s very humbling to know we are helping improve patients’ outcomes.”

Natalia Zielinska Bioskills Laboratory Manager

Smith & Nephew is proud to support surgeons and nurses by enabling them to learn from experts in their field of speciality. We do this at our state-of-the art training and innovation centres. In early 2017 we opened the Expert Connect Centre (‘ECC’) in Croxley Park, Watford, on the outskirts of London, UK. This is already establishing itself as a flagship destination for healthcare professionals from the UK, Europe and the Emerging Markets.

FOCUS ON EMERGING MARKETS

Our Emerging Markets represent those outside the Established Markets, including Brazil, Russia, India and China. The Emerging Markets accounted for 16% of Smith & Nephew's revenue in 2017.

In 2017 we returned our Emerging Markets business to sustainable double-digit revenue growth, up 13% on a reported basis and 12% on an underlying basis. This was a significant improvement over the flat underlying performance of 2016.

In China, our largest Emerging Markets country, we delivered double-digit revenue growth as we improved our commercial execution. In the oil-dependent Gulf States we returned to growth by focusing on securing more private healthcare business to compensate for the reduction in government tenders. The majority of our other Emerging Markets continued to do well across 2017.

We have been early investors in many of the Emerging Markets. There continue to be quarterly fluctuations in the growth rates, and differences in performance between countries, so we look at the longer term trends when making decisions, and those are very favourable.

We also see the next wave of sustained growth coming from the 'mid-tier', essentially growth from widening access to a greater proportion of the population in these countries. We are addressing this by steadily building a dedicated product portfolio and specific distribution model.

We are well positioned to continue to drive strong growth from the Emerging Markets over the medium term. The much improved performance in 2017 is in line with where we see the medium term prospects for this increasingly important segment of Smith & Nephew's business.

$781m
Revenue from Emerging Markets

16%
of Group revenue

+13%	+12%
Reported	Underlying1

WHY THIS KPI IS IMPORTANT

We use this KPI to track the growth of Emerging Markets relative to global growth.

HOW WE PERFORMED

Performance in the Emerging Markets improved strongly over the previous year.

1 These non-IFRS financial measures are explained and reconciled to the most directly comparable financial measure prepared in accordance with IFRS on pages 38 and 178 – 181.

RETURNING CHINA TO GROWTH

“We have seen a return to double-digit growth in the attractive Chinese market.”

Olivier Bohuon Chief Executive Officer

China is our largest Emerging Market country. Here we faced challenges in 2016 as the market growth slowed down. In 2017 we improved our commercial execution and management of, and involvement in, the channel inventory. Looking to the medium term, we believe that our growth prospects in China remain very attractive.

INNOVATE FOR VALUE

In 2017 we began to benefit from a suite of exciting new products, solutions and business models as we deliver on our strategic priority to innovate for value.

In robotics, NAVIO is a unique and compelling system. In 2017 we successfully extended its indications and introduced it to new countries such as India. We launched the total knee arthroplasty (TKA) application for our JOURNEY II, LEGION and GENESIS™ II Total Knee Systems. Surgeons completed the world's first robotics-assisted bi-cruciate retaining total knee replacement procedures. This new approach used NAVIO to implant the new JOURNEY II XR (bi-cruciate retaining total knee system) currently in limited market release. This is the first and only bi-cruciate retaining robotics application commercially available.

In the Emerging Markets we continue to build our mid-tier portfolio. Our ANTHEM™ Total Knee System, which, alongside the ORTHOMATCH™ Universal Instrumentation Platform, has been designed to provide wider market access to affordable knee treatments, performed well following its 2016 launch. During the year we launched into more markets, including Russia and Saudi Arabia, and introduced a new Cruciate Retaining (CR) variant, extending the options available to surgeons.

In Sports Medicine our new LENS™ Surgical Imaging System and WEREWOLF™ COBLATION™ System for resecting soft tissue are being rolled out to customers. In Reconstruction we expanded our REDAPT™ Hip and LEGION™ Knee revision systems. In Advanced Wound Management our pioneering disposable single-use negative pressure wound therapy (sNPWT) device PICO™ continued to perform strongly and we extended our ALLEVYN LIFE foam dressing range with a new non-border version.

We also focus on providing customers with the evidence that demonstrates the effectiveness of our innovative products. In 2017, PICO benefited from new clinical evidence showing its effectiveness at reducing surgical site infections1 and the TRIGEN™ INTERTAN™ hip fracture system also performed strongly supported by new clinical evidence2.

We continue to develop new business models to address changing or unmet customer needs. During 2017 we ran the first study of our innovative Episode of Care Assurance Program (eCAP) that combines our hip and knee implants with PICO and ACTICOAT™ Flex 7 Antimicrobial Barrier Dressings. The first results showed eCAP delivering a 97% decrease in hospital readmission rates following total joint replacement surgery (based on 1,380 joint arthroplasties with only two readmissions, a readmission rate of only 0.145% as compared to published rates of 5.3% or more).

$223m
R&D expenditure

5%
of Group revenue

WHY THIS KPI IS IMPORTANT

Through this KPI we monitor our investment in R&D.

HOW WE PERFORMED

The strong new product portfolio reflects increased investment in R&D and technology acquisitions.

1 O'Leary, D.P. et al, Prophylactic negative pressure dressing use in closed laparotomy wounds following abdominal operations. A randomised, controlled, open-label trial: The PICO Trial. Annals of Surgery, published online 06 December 2016.

2 Smith & Nephew INTERTAN claims brochure "The evidence is in ..."

WORLD-CLASS R&D IN HULL

"Britain is a global leader in medical technology innovation. Partnerships such as this between Smith & Nephew and University of Hull further strengthen our position at the forefront of global medical research and development."

Emma Hardy MP for Hull West & Hessle

In 2017 we announced a long-term partnership with the University of Hull to create one of the world's largest Wound Care Research Clusters with the aim of developing scientific insights and innovative treatments.

This includes the creation of eight PhD studentships and a programme of collaboration between Smith & Nephew's new Hull Research & Development centre and the University's new Health Campus.

SIMPLIFY AND IMPROVE OUR OPERATING MODEL

Since 2011 Smith & Nephew has undertaken two successful efficiency programmes that have delivered significant savings and created an integrated Group structure.

As announced with our Third Quarter 2017 Results, we believe that we now have the Group structure to allow us to strengthen our competitive position by driving further opportunities to accelerate performance through better execution, while at the same time realising savings through greater efficiency.

In 2017 we completed our assessment of these opportunities and started to implement a programme called APEX – Accelerating Performance and Execution in early 2018.

APEX is expected to deliver an annualised benefit of $160 million by 2022, with around three-quarters of this expected by 2020, for a cash cost of up to $240 million, of which a charge of around $100 million is expected in 2018.

APEX has three workstreams:

1. MANUFACTURING, WAREHOUSING AND DISTRIBUTION

We have already made significant improvements over the last two years, and see further opportunities to simplify in line with best practices to reduce overall cost, while improving quality and delivery through:

– A best practice facility footprint with larger manufacturing hubs supported by speciality facilities where appropriate.

– A product portfolio that meets the needs of our customers and complies with regulations, while minimising cost, complexity and inventory.

– A supply chain that is streamlined and efficient so that we are positioned to achieve the highest levels of delivery at benchmark cost.

2. GENERAL AND ADMINISTRATIVE (G&A) EXPENSES

We have improved our G&A expense ratio over the last five years, but with our global function structure we are now able to identify additional areas of opportunity to reduce costs and improve service through:

– Best-in-class Global Business Services that includes a full-spectrum of support services delivered quickly and efficiently, enabling full focus on our customers and business objectives.

– Service hubs in locations that align to our regional needs and deliver the best value for money.

– System infrastructure that drives maximum efficiency, including rationalisation of legacy IT systems and adopting a ‘cloud-first’ strategy.

3. COMMERCIAL EFFECTIVENESS

Whilst the commercial opportunities and competitive environment continue to evolve with changing customer expectations, new go-to-market approaches and price pressure, we expect to improve overall productivity and accelerate top line growth through:

– Increased sales and marketing effectiveness.

– Selective refinement of structures and territories to meet customer and market demands.

– Being more responsive to customers’ use of tenders and changing service level demands.

– More accurate demand forecasting to improve inventory management.

19.6%
Operating Profit Margin

22.0%
Trading Profit Margin1

WHY THIS KPI IS IMPORTANT

We use this KPI to track our underlying profit growth and trading profitability.

HOW WE PERFORMED

Trading profit margin was up 20bps, in line with guidance.

1 These non-IFRS financial measures are explained and reconciled to the most directly comparable financial measure prepared in accordance with IFRS on pages 178–181.

Based on the preliminary work undertaken when I took over as CFO, we undertook a thorough review of our business over the last few months. Our objective was to look afresh at opportunities to strengthen our competitive position and

be more efficient. We have now substantially completed this analysis and begun executing our programmes…"

Chief Financial Officer

A MORE AGILE STRUCTURE

"Based on the preliminary work undertaken when I took over as CFO, we undertook a thorough review of our business over the last few months. Our objective was to look afresh at opportunities to strengthen our competitive position and be more efficient. "We have now substantially completed this analysis and begun executing our programmes…"

Graham Baker Chief Financial Officer

SUPPLEMENT ORGANIC GROWTH WITH ACQUISITIONS

Whilst our focus in 2017 has been on improving our execution across our existing business, we have made one acquisition and a number of strategic agreements that give us access to new technologies.

In 2017 we acquired Rotation Medical, Inc., the developer of a novel tissue regeneration technology for shoulder rotator cuff repair, for an initial cash consideration of $125 million and up to $85 million over the next five years, contingent on financial performance. Its bioinductive implant is highly complementary to our Sports Medicine portfolio, serving an unmet clinical need and providing a compelling new treatment option for our customers2,3,4.

We signed distribution agreements with Leaf Healthcare, a developer of a unique wireless patient monitoring system for pressure ulcer/injury prevention, and MolecuLight i:XTM, a handheld point-of-care imaging device that uses fluorescence imaging to display potentially harmful concentrations of bacteria in wounds in real-time.

2017 marked the third anniversary of our largest acquisition, ArthroCare. This strengthened our Sports Medicine business, with highly complementary product portfolios and customer relationships. ArthroCare also had a strong pipeline of innovations, many of which have been launched since the acquisition. The ArthroCare acquisition has met all of the three-year targets that we set, many ahead of time.

The Board periodically reviews all acquisitions to evaluate longer-term performance and capture lessons learned to help improve strategy and process. Collectively we are pleased with the performance of the technology and Emerging Markets acquisitions we have made. We continue to seek further opportunities to strengthen our technology and product portfolio and Emerging Markets business.

1 These non-IFRS financial measures are explained and reconciled to the most directly comparable financial measure prepared in accordance with IFRS on pages 178–181.

2 Preliminary investigation of a biological augmentation of rotator cuff repairs using a collagen implant: a 2 year MRI follow-up Bokor, Sonnabend, Deady, Cass, Young, Van Kampen, Arnoczky published in Muscles, Ligaments and Tendons Journal 5(3):144 150 (2015).

3 Histologic Evaluation of Biopsy Specimens Obtained After Rotator Cuff Repair Augmented With a Highly Porous Collagen Implant Arnoczky, D.V.M., Shariff K. Bishai, D.O., M.S., F.A.O.A.O., Brian Schofield, M.D., Scott Sigman, M.D., Brad D. Bushnell, M.D., M.B.A., Jan Pieter Hommen, M.D., and Craig Van Kampen, Ph.D. Arthroscopy: The Journal of Arthroscopic and Related Surgery, 33(2):278 283 (2016).

4 Evidence of healing of partial-thickness rotator cuff tears following arthroscopic augmentation with a collagen implant: a 2 year MRI follow-up. Bokor, Sonnabend, Deady, Cass, Young, Van Kampen, Arnoczky. Muscles, Ligaments and Tendons Journal 6(1):16 25 (2016).

ARTHROCARE

In 2014 we acquired ArthroCare for $1.5 billion to strengthen our Sports Medicine business through complementary product portfolios and customer relationships.

$50m+
of additional
sales from
cross-selling
$85m
of total
synergies on
trading
profit1 level

WHY THIS KPI IS IMPORTANT

We use this KPI to demonstrate the returns from acquisitions.

HOW WE PERFORMED

ArthroCare has met or exceeded all of the three-year targets, many ahead of time. We achieved both the cost and revenue synergies totalling $85m on a trading profit1 level, and the Return on Invested Capital in year three exceeded our target.

STRENGTHENING SPORTS MEDICINE

“We are proud of the impact our technology has made in healthcare and are excited by the opportunity to reach many more customers and their patients as an integrated part of Smith & Nephew’s extensive Sports Medicine portfolio.”

Martha Shadan Chief Executive Officer, Rotation Medical, Inc.

The bioinductive implant from Rotation Medical, Inc. has shown the ability to heal by inducing the growth of new tendon-like tissue2,3,4. With its small sales force, Rotation Medical, Inc. achieved revenue of $17m in 2017.

We expect rapid growth as we roll out the product across our large Sports Medicine sales force, first focusing on the US where the product has FDA approval.

OUR MARKETPLACE

ATTRACTIVE
LONG-TERM TRENDS

$34 billion
Smith & Nephew's addressable segment in medical devices1

4%
Annual growth rate of Smith & Nephew's addressable segment1

HEALTHY FUNDAMENTALS, BUT COST REMAINS AN ISSUE

According to a study commissioned by the Bill and Melinda Gates Foundation (Lancet, April 2017) global healthcare spend, amounting to c. $9 trillion in 2014, is set to grow at a real rate of c. 3% per annum per capita, reaching c. $16 trillion in 2030 and c. $24 trillion in 2040, representing c. 8% of the global economy.

The medical devices and supplies segment of healthcare is today worth approximately $340 billion per annum. Within that, Smith & Nephew's addressable segment is approximately $34 billion, growing at around 4% annually.

The main drivers for healthcare demand include demographic shift towards older populations, increases in lifestyle related ailments such as obesity, advances in technology leading to increased scope for treatment, and economic growth increasing the access and demand for healthcare – especially in the Emerging Markets. Additionally, patients increasingly seek to influence the choice of care as they become more and more informed about the range and nature of treatment options available.

Today healthcare expenditure already constitutes a significant share of the overall global economy, especially in developed markets where populations are ageing rapidly. As an example, the share of US GDP spent on healthcare has reached nearly 17% and is set to continue to rise (Lancet, April 2017). As a result, cost and cost control remain the

dominant issues across the sector and healthcare systems increasingly shift towards more efficient and effective value-based care.

SHIFT TOWARDS VALUE RATHER THAN VOLUME

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

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

As an example, the US Centers for Medicare & Medicaid Services (CMS) aims by 2018 to spend 50% of its Medicare fee-for-service payments through alternative payment models and link 90% of its fee-for-service to quality (CMS, Jan 2015).

FOCUS ON LOWERING COSTS AND INCREASING EFFICIENCY

The desire to lower costs and increase efficiency gives rise to several trends including, for example: healthcare providers increasingly seeking to treat patients in outpatient or community settings; the increasing use of digital technologies to ensure that care is as efficient and effective as possible; the acceptance of ‘good enough’ products in some circumstances; and the sector increasingly seeing efforts to cooperate across the value chain. As an example, the UK National Health Service (NHS) is automating data exchange between its institutions and suppliers and has mandated all suppliers to provide pricing information through the Global Data Synchronization Network (GDSN) by October 2018 (NHS, Feb 2016).

GOVERNMENTS, REGULATIONS & COMPLIANCE

Governments and other public bodies are key stakeholders in our marketplace.

In the US, where healthcare spending is higher as a percentage of GDP than most other countries, politicians and regulators are focused on reducing cost and simplifying the regulatory burden on the industry. Although common ground is hard to find, there is a general consensus that the US healthcare system needs to be restructured.

In 2017, the European Union reached agreement on a new set of Medical Device Regulations which entered into force on 25 May 2017. These have a three-year transition period; therefore will fully apply in EU Member States from 26 May 2020. These regulations will impose tougher requirements of market entry and post market surveillance of medical devices. Although healthcare systems are less costly in Europe than in the US, strained government budgets and demographic challenges are driving an increased focus on value-based healthcare and requirements to demonstrate the value of innovation through evidence. Additionally, some uncertainty exists around the UK's exit from the European Union where the regulatory impact is not yet clear.

In China, which in recent years has focused on, and succeeded with, increasing access to healthcare, there is a strong focus on compliance and cost control. In 2017 the country introduced the two invoices system which effectively limits length of the supply chain thus increasing transparency and lowering cost to the end consumer. Also in 2017 Chinese regulators initiated a process to lower prices on medical devices. The initial focus of these efforts is on hip implants, drug-eluting stents and implantable cardioverter-defibrillators (ICDs).

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

Legislation covering corruption and bribery, such as the UK Bribery Act and the US Foreign Corrupt Practices Act, applies to all our global operations. We, and other companies in the industry, are subject to regular inspections and audits by regulatory agencies and notified bodies, and in some cases remediation activities have required, and will continue to require, significant financial and resource investment.

SEASONALITY

Orthopaedic reconstruction and sports medicine procedures tend to be higher in the winter months when accidents and sports related injuries are highest. Elective procedures tend to slow down in the summer months due to holidays. Due to the nature of our product range, there is little seasonal impact on our Advanced Wound Management franchises.

In the US, out-of-pocket costs for health insurance plans are tied to medical expenses in a calendar year. As a result, households who have reached their deductible (or out-of-pocket) cap may find that accessing care later in the year comes at a lower cost, which can encourage more of them to try and schedule any required treatments or procedures in the final months of any given year.

COMPETITION

Across our franchises we have a number of competitors which differ with respect to both product focus, geographic reach and overall scale. Whereas our key surgical competitors are generally larger and more exposed to the US, our key wound competitors are generally not US centric.

In Orthopaedic Reconstruction and Trauma we are one of four leading players as we compete against Stryker (US), Zimmer Biomet (US) and Johnson & Johnson (US). In Sports Medicine we hold a leading position behind Arthrex, while also competing against the aforementioned companies.

Our Advanced Wound Management business is the second largest in our marketplace. We lead the somewhat fragmented Advanced Wound Care sub-segment alongside Mölnlycke (Sweden). In Advanced Wound Devices we are the primary challenger to US based NWPT incumbent Acelity (US). In Advanced Wound Bioactives our key products lead their respective categories.

MARKET SIZE1

$5.5bn +6% Sports Medicine2		$8.5bn +5% Advanced Wound Management		$14.5bn +2% Hip & Knee Implants (Recon)		$5.5bn +4% Trauma & Extremities	
A SMITH & NEPHEW	22%	A SMITH & NEPHEW	15%	A SMITH & NEPHEW	11%	A SMITH & NEPHEW	9%
B ARTHREX	32%	B ACELITY	17%	B ZIMMER BIOMET	31%	B DEPUY SYNTHES3	45%
C DEPUY (MITEK)3	14%	C MOLNLYCKE	10%	C DEPUY SYNTHES3	23%	C STRYKER	26%
D STRYKER	11%	D CONVATEC	7%	D STRYKER	20%	D ZIMMER BIOMET	11%
E OTHERS	21%	E OTHERS	51%	E OTHERS	15%	E OTHERS	9%

1 Data used in 2017 estimates generated by Smith & Nephew is based on publicly available sources and internal analysis and represents an indication of market shares and sizes.

2 Representing access, resection and repair products.

3 A division of Johnson & Johnson.

OUR PRODUCTS

THE PRODUCTS WE TAKE TO MARKET

Smith & Nephew has nine global product franchises

A	KNEE IMPLANTS	$984m
B	HIP IMPLANTS	$599m
C	TRAUMA & EXTREMITIES	$495m
D	SPORTS MEDICINE JOINT REPAIR	$627m
E	ARTHROSCOPIC ENABLING TECHNOLOGIES	$615m
F	OTHER SURGICAL BUSINESSES	$189m
G	ADVANCED WOUND CARE	$720m
H	ADVANCED WOUND BIOACTIVES	$342m
I	ADVANCED WOUND DEVICES	$194m

KNEE IMPLANTS

2017 revenue

$984m

Reported	Underlying1
+6%	+5%

Smith & Nephew offers an innovative range of products for specialised knee replacement procedures. Knee replacement surgery involves replacing the worn, damaged or diseased portion of a knee with an artificial joint. Every year more than two million patients receive total, partial or revision knee replacements worldwide.

Smith & Nephew's knee systems include the LEGION/GENESIS II Total Knee System, a comprehensive system designed to allow surgeons to address a wide range of knee procedures, and our JOURNEY II family of Active Knees. The anatomical shape of the JOURNEY II is designed to reproduce normal knee kinematics and thereby delivers

improved functional outcomes and high patient satisfaction.

In 2017 we progressed the limited market release of our JOURNEY II XR, an innovative bi-cruciate retaining knee implant, which is designed to retain the anterior and posterior cruciate ligaments (ACL/PCL) and deliver normal perception of movement and muscle control2.

These systems also feature VERILAST™ Technology, our advanced bearing surface. The LEGION Primary Knee with VERILAST Technology has been laboratory-tested to 30 years of simulated wear. While lab testing is not the same as clinical performance, the tests showed significant reduction in wear compared to conventional technologies.

Our knee systems utilise our VISIONAIRE™ Patient-Matched Instrumentation, whereby a patient's MRI and X-Rays are used to create customised cutting guides that allow the surgeon to achieve optimal alignment of the new implant.

In 2017 we expanded the geographic scope of the ANTHEM Total Knee System, which, alongside the ORTHOMATCH Universal Instrumentation Platform, has been designed to provide a wider market access to affordable knee treatment. ANTHEM is tailored to meet the anatomical needs of patients from Asia, the Middle East, Africa and Latin America and the ORTHOMATCH instrumentation platform reduces weight, footprint and unnecessary cost without compromising on quality or clinical outcomes. In 2017 we expanded the geographic scope of the system which is now available in many markets including India, South Africa, Mexico, Colombia, Chile, Russia and the Middle East. We began the limited market release of a cruciate retaining version in 2017.

In early 2017 we launched the NAVIO Total Knee Arthroplasty (TKA) system, adding to the indications offered on our leading robotics platform. In the fourth quarter, we initiated the limited market release for the NAVIO XR system, which we believe will be a key technology enabler for the JOURNEY II XR knee. The robotics team continues to expand to major geographies such as India, South Africa and Australia. For more information on NAVIO see page 22.

In 2017 performance in this franchise was driven by strong demand for the JOURNEY II Total Knee System supported by growth from the LEGION Revision Knee System and ANTHEM Total Knee System.

1 These non-IFRS financial measures are explained and reconciled to the most directly comparable financial measure prepared in accordance with IFRS on pages 178–181.

2 Moro-Oka, Taka-Aki, Marc Muenchinger, Jean Pierre Canciani, and Scott A Banks. 'Comparing in Vivo Kinematics of Anterior Cruciate-retaining and Posterior Cruciate-retaining Total Knee Arthroplasty'. Knee Surgery, Sports Traumatology, Arthroscopy 15.1. (2007):93:99 Web.

RENEWING
ACTIVE LIFESTYLE

Today’s fastest growing segment of knee replacement patients is seeking a return to a more active lifestyle1

Traditional knee replacement options don’t meet the need for higher functionality, improved motion or long-term durability2,3,4,5. Most significantly, these systems fall short in providing a return to a normal pattern of motion meaning less satisfaction for patients.

For orthopaedic surgeons seeking treatment solutions beyond traditional knee replacements, JOURNEY II Active Knee Solutions have been engineered to empower patients to return to an active lifestyle.

JOURNEY II is a seamless, next generation family of partial and primary knee designs, including a new bi-cruciate retaining JOURNEY II XR. JOURNEY II is intended to restore patients to an unmatched level of function, motion and durability.

HIP
IMPLANTS
2017 revenue
0% 0%
$599m
Reported Underlying1

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

For Hip Implants, Smith & Nephew has developed a range of primary hip systems. Core systems include the ANTHOLOGY™ Hip System, SYNERGY™ Hip System, the POLARSTEM Femoral Hip System, the R3 Acetabular System and the POLARCUP™ Dual Mobility Hip System. This diversity exemplifies our commitment to providing surgeons with implant and instrumentation options that meet the specific demands of their patients and preferred

surgical approach, most notably the direct anterior or posterolateral approach.

We also market the BIRMINGHAM HIP Resurfacing (BHR) System, an important option for surgeons treating suitable patients.

Smith & Nephew's portfolio also includes the REDAPT Revision Femoral System.

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

The REDAPT Revision Femoral System comprises a monolithic stem and a Fully Porous Shell. A Fully Porous Acetabular Cup with CONCELOC™ Technology was introduced in 2016. To allow ingrowth, an additive, or 3D printing, manufacturing process is used to produce an entirely porous implant that mimics the structure of cancellous bone. The 3D printing method allows for complex design geometries that would be difficult, expensive or impossible to achieve with traditional manufacturing methods. For example, solid reinforcements can be built directly into the porous structure to provide extra strength in precise locations.

In 2017 we introduced a number of REDAPT Augments to be used in conjunction with the fully porous shell which will allow surgeons to treat more difficult acetabular revisions.

In 2017 performance in this franchise was better in the second half of the year, driven by new REDAPT Revision and POLARSTEM Cementless Stem systems.

1 These non-IFRS financial measures are explained and reconciled to the most directly comparable financial measure prepared in accordance with IFRS on pages 178–181.

RENEWING ACTIVE LIFESTYLE

1 US Department of Health and Human Services Agency (HHSA) for Healthcare Research and Quality (AHRQ) Knee Replacements Up Dramatically Among Adults 45 to 64 Years Old. AHRQ News and Numbers, November 3, 2011. Agency for Healthcare Research and Quality, Rockville, MD.

2 Phil Noble et al; Does total knee replacement restore normal knee function? 2005; CORR. (431): 157 65.

3 Huch K, Müller KA, Stürmer T, Brenner H, Puhl W, Günther KP. Sports activities 5 years after total knee or hip arthroplasty: the Ulm Osteoarthritis Study. Ann Rheum Dis. 2005 Dec; 64 (12):1715 20.

4 Comparing patient outcomes after THA and TKA: is there a difference? Bourne RB, Chesworth B, Davis A, Mahomed N, Charron K. Clin Orthop Relat Res. 2010 Feb; 468(2):542 6. Epub 2009 Sep 4.

5 Functional comparison of posterior cruciate-retained versus cruciate-sacrificed total knee arthroplasty. Dorr LD, Ochsner JL, Gronley J, Perry J. Clin Orthop Relat Res. 1988 Nov; (236):36.

TRAUMA & EXTREMITIES

2017 revenue

+4% +4%

$495m

Reported Underlying1

Our Trauma & Extremities franchise supports healthcare professionals by pioneering solutions for surgeons to stabilise severe fractures, correct bone deformities, treat arthritis, and heal soft tissue complications.

For Trauma, the principal internal fixation products are the TRIGEN family of intramedullary (IM) nails (TRIGEN META-NAIL System, TRIGEN Humeral Nail System and TRIGEN INTERTAN), EVOS™ Plating System and the PERI-LOC™ Plating System. In 2016 we unveiled new evidence showing that the TRIGEN INTERTAN hip fracture system allows patients to experience lower risk of implant failure and re-operation; faster time to fracture union; and a high return to pre-fracture status2.

The EVOS Mini Fragment Plate and Screw System is a dedicated Trauma mini fragment system. This is a stainless steel highly versatile system with a multitude of plate geometries and longer screw lengths than standard mini fragment systems. In 2017, we introduced the EVOS Small Fragment system for lower extremity fractures and general trauma utilisation. This new system features more points of fixation and greater breadth of plate options. EVOS Small takes an evolutionary approach to simplifying and unifying small fragment plating systems.

For extremities and limb restoration, we offer the TAYLOR SPATIAL FRAME™ Circular Fixation System as well as a range of plates, screws, arthroscopes, instrumentation, resection and suture anchor products including foot and ankle and hand and wrist specialists. In addition, we introduced INVISIKNOT™, a unique syndesmotic fixation device for the ankle.

2017 saw the global launch of the ATLAS™ Hip Fracture Nail in South Africa and India. It is the first Smith & Nephew nail specifically designed for the Emerging Markets.

In 2017 performance in this franchise was driven by growth from our TRIGEN INTERTAN hip fracture system where new clinical evidence continued to support increased uptake.

1 These non-IFRS financial measures are explained and reconciled to the most directly comparable financial measure prepared in accordance with IFRS on pages 178–181.

2 Smith & Nephew INTERTAN claims brochure “The evidence is in ...”

SPORTS MEDICINE JOINT REPAIR
2017 revenue

	Reported	Underlying1
$627m	+7%	+6%

Our 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 the repair of soft tissue injuries and degenerative conditions of the knee, hip and shoulder. Our franchise operates in a large, growing market where unmet clinical needs lend room for procedural and technological innovation. Smith & Nephew is well positioned both to innovate and to reach customers globally.

Key products for knee repair include the FAST-FIX™ family of meniscal repair systems, the ENDOBUTTON™ and ULTRABUTTON™ fixed and adjustable loop devices for knee ligament reconstruction, BIOSURE™ interference screws for ligament procedures, and CARGELTM for the repair of articular cartilage.

FIRST AND ONLY

First and only bi-cruciate retaining robotics application

2017 saw the world’s first robotics-assisted bi-cruciate retaining total knee replacement procedures, utilising our NAVIO robotics-assisted surgical system and the JOURNEY II XR bi-cruciate retaining total knee system.

The JOURNEY II XR has the potential to deliver the best possible outcome for the surgeon and patient through the preservation of important anatomical structures such as the Anterior Cruciate Ligament (ACL). The NAVIO robotics-assisted surgical system enables accurate tibial implant placement to deliver a more reproducible surgical technique. We are proud to be the only company to offer the unique combination of NAVIO robotics-assistance and the JOURNEY II XR Knee System.

For shoulder, Smith & Nephew markets a suite of products for Rotator Cuff Repair (RCR), one of the most common sports medicine procedures. These include ULTRATAPE™, a suture that provides greater tendon-to-bone contact when compared to traditional #2 suture and may enhance repair2, FIRSTPASS™ ST, a sterile-packaged retrograde suture passer that eliminates the steps of loading and unloading needles and cartridges; MULTIFIX™ S, an all-PEEK knotless screw-in anchor; and HEALICOIL™, a family of suture anchors featuring open architecture that allows new bone to fill the fenestrations between screw threads. All these products can be used together or in conjunction with other existing products from the Smith & Nephew portfolio in a single procedure, significantly expanding the breadth of our RCR Solutions.

In 2017 we acquired Rotation Medical, Inc., the developer of a novel tissue regeneration technology for RCR, for an initial cash consideration of $125 million and up to $85 million over the next five years, contingent on financial performance. The Rotation Medical Rotator Cuff System incorporates a breakthrough technology and technique that balances biomechanics and biology to enhance the body's natural healing response, helping tendons heal by inducing growth of new tendon-like tissue4,5,6. Rotation Medical is highly complementary to our Sports Medicine portfolio, serving an unmet clinical need and providing a compelling new treatment option for our customers.

The Smith & Nephew joint repair portfolio includes two next-generation anchors made of soft, all-suture material – Q-FIX™ and SUTUREFIX™. The Q-FIX All-Suture Anchor is ideal for a variety of arthroscopic shoulder and hip repairs, offering fixation performance superior to commonly used all-suture anchors and traditional anchors7,8. The SUTUREFIX Ultra anchor is an attractive option for procedures in which anatomic space is very limited9 while still delivering high fixation strength10,11,12.

Smith & Nephew offers joint repair implants made from REGENESORB™, including versions of the HEALICOIL™ suture anchors for shoulder repair and BIOSURE™ interference screws for knee repair. REGENESORB™ is an advanced biocomposite material shown to be absorbed and completely replaced by bone within 24 months in pre-clinical studies13,14.

Smith & Nephew supports specific joint repair procedures for shoulder, knee and hip with a line of instruments, positioners and holders, including SPIDER2™/T-MAX procedure-enabling limb positioning systems and ACUFEX™ Hand Held Instruments.

In 2017 performance in this franchise was driven by strong demand for our leading shoulder repair portfolio.

ARTHROSCOPIC
ENABLING TECHNOLOGY
2017 revenue

Reported	Underlying1
-3%	-3%

$615m

Our Arthroscopic Enabling Technologies (AET) franchise includes high definition imaging solutions, industry leading energy based and mechanical resection platforms, and fluid management and access portfolios.

AET platforms work in concert to facilitate access to various joint spaces, visualise the patient's anatomy, resect degenerated or damaged tissue and prepare the joint for a soft tissue repair. Products in this franchise are often used in conjunction with products from our Sports Medicine Joint Repair franchise.

Key AET products include the LENS™ Integrated visualisation system which provides outstanding image quality and functionality in a simple three-in-one Console (CCU, LED Light Source and Image Management System), Camera Head and iPad application.

We also offer the WEREWOLF and QUANTUM™ 2 COBLATION™ controllers and a wide range of high performance COBLATION Technology radio frequency (RF) wands to precisely ablate, resect and coagulate soft tissue and enable haemostasis of blood vessels.

The WEREWOLF COBLATION System is the latest innovation in our market-leading COBLATION technology. Featuring an all new controller and designed to support a broad variety of wands, WEREWOLF delivers an unparalleled range of performance capabilities and advanced safety features – WEREWOLF carries broad indications across Sports Medicine.

DYONICS™ Shaver blades provide superior resection due to their sharpness and reduce clogging with their debris evacuation capabilities, GoFLO™ and Double® Pump RF fluid management consoles expand the joint space while providing haemostasis and maintaining the saline environment necessary to perform arthroscopic procedures.

Within an operating room, our AET products are typically kept together in an arthroscopic tower, often comprising a visualisation or camera system, COBLATION or energy based resection controllers, mechanical resection or blade controllers and fluid management or pump components. Because of the strong link between the arthroscopic tower and consumables, we will showcase our industry leading tower components, such as LENS, COBLATION and DYONICS shaver blades, when selling the broader Sports Medicine portfolio.

In 2017 performance in this franchise was impacted by continued softness in mechanical resection and the legacy RF technology during the year. Our new LENS visualisation system and WEREWOLF COBLATION system are growing in share within our portfolio and we expect a gradual improvement in 2018.

1 These non-IFRS financial measures are explained and reconciled to the most directly comparable financial measure prepared in accordance with IFRS on pages 178–181.

2 Shive, M., MD, et al. BST-CarGel Treatment Maintains Cartilage Repair Superiority over Microfracture at 5 Years in a Multicenter Randomized Controlled Trial. Cartilage 2015; Vol 6(2) 62 72.

3 Potter L, Moore C. Increased contact area utilizing the ULTRATAPE Suture for rotator cuff repair. Bone&JointScience: Our Innovation in Focus. 2014;4(3):1 4. Lit no: 02056.

4 Preliminary investigation of a biological augmentation of rotator cuff repairs using a collagen implant: a 2 year MRI follow-up Bokor, Sonnabend, Deady, Cass, Young, Van Kampen, Arnoczky published in Muscles, Ligaments and Tendons Journal 5(3):144 150 (2015).

5 Histologic Evaluation of Biopsy Specimens Obtained After Rotator Cuff Repair Augmented With a Highly Porous Collagen Implant Arnoczky, D.V.M., Shariff K. Bishai, D.O., M.S., F.A.O.A.O., Brian Schofield, M.D., Scott Sigman, M.D., Brad D. Bushnell, M.D., M.B.A., Jan Pieter Hommen, M.D., and Craig Van Kampen, Ph.D. Arthroscopy: The Journal of Arthroscopic and Related Surgery, 33(2):278 283 (2016).

6 Evidence of healing of partial-thickness rotator cuff tears following arthroscopic augmentation with a collagen implant: a 2 year MRI follow-up. Bokor, Sonnabend, Deady, Cass, Young, Van Kampen, Arnoczky. Muscles, Ligaments and Tendons Journal 6(1):16 25 (2016).

7 ArthroCare Report #P/N 54231 01 Rev. A; ArthroCare Report #P/N 49193 01 Rev. A; ArthroCare Report #P/N 51963 01 Rev. A.

8 Douglass NP, Behn AW, Safran MR. Cyclic and Load to Failure Properties of All-Suture Anchors in Synthetic Acetabular and Glenoid Cancellous Bone. Arthroscopy (26 January 2017).

9 Smith & Nephew Evaluation Reports 15002113, 15002112, 15002117.

10 Smith & Nephew 2011. Validation REPORT ULTRABRAID II SUTURE – BIOCOMPATIBILITY – 15001076.

11 Smith & Nephew 2013. Competitive Claims REPORT, SutureFix – 15002059.

12 Smith & Nephew 2013. Validation REPORT, Hip Suturefix XL – 15001076.

13 Data on File, Smith & Nephew report 15000897.

14 Results of in vivo simulation have not been shown to quantitatively predict clinical performance.

OTHER SURGICAL BUSINESSES

2017 revenue

$189m

Reported2	Underlying1
-11%	+7%

The Other Surgical Businesses franchise includes our Ear, Nose & Throat (ENT) business and the NAVIO robotic surgical business, acquired at the start of 2016.

In ENT we offer surgeons a wide variety of market leading technologies to address some of the most common pathologies in otolaryngology. Our COBLATION technology has been used to remove tonsils and adenoids for over 15 years and is preferred by surgeons and patients for its ability to remove tissue at low temperatures with minimal damage to surrounding tissue.

With its ease of use and strong clinical history, COBLATION Technology is also marketed for use in turbinate and laryngeal procedures.

Our RAPID RHINO™ Carboxymethylcellulose (CMC) Technology is featured in both dissolvable and removable nasal and sinus dressings and epistaxis treatment products. When mixed with water, CMC forms a cushioning gel that naturally drains from the body after several days and supports healing by maintaining a moist physical environment.

The NAVIO Surgical System is a next generation handheld robotics platform designed to aid surgeons with implant alignment, ligament balancing and bone preparation. Furthermore, the NAVIO robotics-assisted system does not require a preoperative image, such as a CT scan. This allows patients to receive the benefits of robotics-assistance without the extra steps, costs and radiation associated with additional preoperative imaging.

In 2017 we successfully expanded the NAVIO platform into total knees, which comprise 80% of all knee replacement surgeries globally. The total knee arthroplasty (TKA) application supports Smith & Nephew’s JOURNEY II, LEGION Primary and GENESIS II Total Knee Systems.

Also during 2017 surgeons completed the world’s first robotics-assisted bi-cruciate retaining total knee replacement procedures. With this launch, NAVIO now offers both partial and total knee options that include the first and only robotics-assisted bi-cruciate retaining knee procedure, commercially available today.

In 2017 performance in this franchise was driven by the Ear, Nose & Throat business and continued demand for our hand-held robotics NAVIO Surgical System including the new Total Knee Application. The decline in reported

revenues reflects the impact of the disposal of the Gynaecology business in 2016.

ADVANCED
WOUND CARE
2017 revenue
0% 0%
$720m
Reported Underlying1

The Advanced Wound Care (AWC) franchise consists of several groups of brands, including exudate management, infection management and our cornerstone range of products.

Exudate management products focus on providing appropriate wound fluid absorption and evaporation properties to promote an optimal wound healing environment. This will reduce the burden a wound has on the patients and help them to get on with their lives and at the same time diminish costs for materials and nursing time.

Our key growth brand in this space is ALLEVYN LIFE, an innovative dressing designed to improve the quality of life for patients with chronic wounds, as well as helping healthcare professionals reduce the costs of frequent dressing changes. Further research was published in 2017, with a Randomised Controlled Trial (RCT) showing how the use of ALLEVYN LIFE, when combined with standard care, reduced the rate of pressure ulcers in the sacrum by 71%3.

Silver and iodine drive our infection management portfolio.

Our silver-based products (ACTICOAT, DURAFIBER™ Ag and ALLEVYN Ag) provide clinicians with a range of solutions to address individual patient needs in managing wound infection. ACTICOAT is well positioned to address the need for highly effective, fast-acting local antimicrobials in the care of serious infection on a wide range of wounds, including surgical incisions and chronic wounds.

Our cadexomer iodine based product, IODOSORB™, has a unique mode of action to deliver low level, slow release elemental iodine without cytotoxic effects and effectively eradicates biofilms. A recent expert consensus showed biofilms contribute to the delay in healing of chronic wounds4.

Smith & Nephew's cornerstone range offers a wide selection of 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.

OPSITE™ is one of our most pioneering products and has become the global standard of care in post-operative dressings. IV3000™, a specialist premium dressing for intravenous lines, continues to perform well. PROSHIELD™ & SECURA™ are proven preventative skin care products which help maintain and protect skin integrity.

In 2017 performance in this franchise was impacted by softer market conditions in Europe, which offset strong growth in the US.

1 These non-IFRS financial measures are explained and reconciled to the most directly comparable financial measure prepared in accordance with IFRS on pages 178–181.

2 Reflects reduction in revenue following sale of Gynaecology business in 2016 (2016 Gynaecology revenue: $37m).

3 Forni C., D'Alessandro F., Gallerani P., Genco R., Bolzon A,, Bombino C., Mini S., Rocchegiani L., Notarnicola T., Vitullia A., Amodeo A., Celli G. Effectiveness of Using a New Polyurethane Foam Multi-layer Dressing in the

Sacral Area to Prevent the Onset of Pressure Ulcer in the Elderly with Hip Fractures. Poster presented at EPUAP 2017.

4 Schultz G., Bjarnsholt T., James G. A., Leaper D. J., McBain A. J., Malone M., Stoodley P., Swanson T., Tachi M., Wolcott R. D. for the Global Wound Biofilm Expert Panel. Consensus guidelines for the identification and treatment of biofilms in chronic non-healing wounds International Journal of Tissue Repair and Regeneration (in press).

OWN THE DISEASE

Helping customers get closer to zero...

Smith & Nephew supports healthcare professionals in reducing the human and economic cost of wounds through pioneering solutions that improve outcomes and at the same time conserve resources for health systems. Our aim is to help our customers get closer to zero surgical site complications, pressure ulcer incidence, delay in wound healing, diabetic foot amputations, and waste of healthcare. Customer insights have confirmed the need to augment our treatment offering with solutions that support the clinician in making informed decisions and achieving consistency of practice.

In 2017 we entered two distribution relationships for innovative products in the Pressure Ulcer Prevention and Infection Management categories – Leaf and MolecuLight i:X – which extended our solutions beyond treatment options.

LEAF

An estimated 2.5 million pressure ulcers/injuries are treated each year in US acute care facilities alone1, with the cost to treat a single full thickness pressure ulcer/injury as high as $70,0002 and an estimated annual burden of $11 billion3. Proven prevention strategies focus on protecting vulnerable areas, maintaining skin integrity and consistent offloading through patient turning.

However, despite the best efforts, maintaining these schedules with a consistent execution is often difficult. In particular, turning regimes for patients at high risk can be difficult to adhere to, going against the latest best practice guidance. The Leaf Patient monitoring system is a patient worn wireless sensor which monitors the patient’s position. The constant processing of the positional data facilitates real time alerts to patient needs and turning schedules. This data can help reduce the incidence of hospital-acquired pressure injuries and help improve operational efficiency as part of a full protocol of care.

In an independently conducted RCT4 evaluating optimal patient turning, Leaf induced a 43% relative increase in turning protocol compliance in high-risk patients. Patients treated with Leaf were 73% less likely to develop a pressure injury.

MOLECULIGHT i:X

Currently wound assessments are made with the naked eye which can lack the accuracy required to most effectively guide clinical decision making.5 Using fluorescence, MolecuLight i:X quickly, safely, and easily visualises potentially harmful bacteria6,7,8 in wounds which may otherwise lack signs or symptoms of infection. It enhances a clinician’s ability to choose the right therapy, at the right time for their patient6,7 and can help to guide wound sampling and

debridement6,9,10, monitor wound progression7,8, improve patient engagement5,9 and simplify wound documentation6.

Clinical data from wound assessments demonstrates that incorporating the MolecuLight i:X into standard of care facilitated more objective medical decision making and led to up to nine times faster wound healing6 and 54% more accurate swabbing.11 MolecuLight i:X is not yet available in the US.

1 Sen et al. Wound Rep Reg 2009. 17:763 771.

2 Reddy et al. Preventing Pressure Ulcers: A Systematic Review. JAMA, August 23/30 2006 Vol 296, No 8 (Reprinted).

3 Russo et al. Hospitalizations Related to Pressure Ulcers, 2006. HCUP Statistical Brief #64. December 2008. Agency for Healthcare Research and Quality, Rockville, MD. http://www.hcup-us.ahrq.gov/reports/statbriefs/sb64.pdf.

4 Pickham D. et al. Effect of a wearable patient sensor on care delivery for preventing pressure injuries in acutely ill adults: A pragmatic randomized clinical trial (LS-HAPI study). International Journal of Nursing Studies 80 (2018) 12–19.

5 Hoeflok J et al. Pilot clinical evaluation of surgical site infections with a novel handheld fluorescence imaging device. Proceedings of the Annual Military Health System Research Symposium (MHSRS); 2014 Aug 18–21; Fort Lauderdale, FL.

6 DaCosta RS et al. Point-of-care autofluorescence imaging for real-time sampling and treatment guidance of bioburden in chronic wounds: first-in-human results. PLoS One. 2015 Mar 19;10(3).

7 MolecuLight Inc. PN 1189 MolecuLight i:X User Manual. 2016.

8 MolecuLight Inc. Case Study 0051 Track Wound Size and Bacterial Presence with the MolecuLight i:X. 2016.

9 Raizman R. Point-of-care fluorescence imaging device guides care and patient education in obese patients with surgical site infections. Presented at: CAWC 2016. Proceedings of the Annual Canadian Association of Wound Care Conference (CAWC); 2016 Nov 3 6, Niagara Falls, ON.

10 Raizman R. Fluorescence imaging positively predicts bacterial presence and guides wound cleaning and patient education in a series of pilonidal sinus patients. Proceedings of the Annual Wounds UK Conference; 2016 Nov 14 16; Harrogate, UK.

11 Ottolino-Perry K et al. Improved detection of wound bacteria using fluorescence image guided wound sampling in diabetic foot ulcers. Int Wound J. 2017 Feb 28. doi: 10.1111/iwj.12717.

ADVANCED
WOUND BIOACTIVES
2017 revenue

0%	0%
$342m	
Reported	Underlying1

Our Advanced Wound Bioactives (AWB) franchise focuses on the commercialisation of novel, topical biologic and skin substitute products that provide a unique approach to debridement, dermal repair and tissue regeneration.

Currently, our AWB portfolio includes Collagenase SANTYL Ointment (the only FDA-approved biologic enzymatic debriding agent for chronic dermal ulcers and severe burns), OASIS® Wound Matrix and Ultra Tri-Layer Matrix (naturally-derived, extracellular matrix replacement products indicated for the management of both chronic and traumatic wounds) and REGRANEX® (becaplermin) Gel 0.01% (an FDA-approved platelet-derived growth factor for the treatment of lower extremity diabetic neuropathic ulcers).

Our most significant product by sales is SANTYL Ointment, which plays an integral role in removing necrotic or dead tissue in chronic dermal ulcers (such as pressure ulcers, diabetic ulcers, and venous ulcers) and severely burned patients.

SANTYL Ointment is often considered as the reference debridement product, especially in the hospital and nursing home markets. Additionally, in 2017 we continued to see growth in the use of SANTYL Ointment by office-based physicians and have been able to stabilise the nursing home market.

We continue to focus on further establishing the value of SANTYL Ointment in treating patients. We are also working to lower overall treatment costs, improve outcomes and patient satisfaction, and further educate physicians, patients, and payers on the critical role that SANTYL Ointment plays in moving patients forward through the healing process.

The wound bioactives market growth continues to be impacted by changes in the reimbursement landscape that are driving increases in out-of-pocket expenses for patients and access in general across all sites of care.

The US is the largest market and represents the current focus for our AWB franchise. SANTYL Ointment is also available in Canada. OASIS is accessible in a number of other Established Markets.

In 2017 performance in this franchise reflected SANTYL returning to growth in the second half of the year as it benefited from new analysis of its effectiveness in advancing pressure ulcers through the healing process offset by the

reimbursement environment for OASIS which remained a headwind, as expected.

ADVANCED
WOUND DEVICES
2017 revenue

Reported	Underlying1
+13%	+13%

$194m

Our Advanced Wound Devices (AWD) franchise is comprised of our Negative Pressure Wound Therapy (NPWT) and surgical debridement businesses.

The PICO system, our pioneering single-use, canister-free NPWT solution brings the effectiveness of traditional NPWT in a modern, small portable system2. It is designed for both open wounds such as pressure ulcers and closed incisions and leverages our leading dressing technology.

In 2017 the evidence base supporting PICO in our target surgical indications continued to build. A Level 1 meta-analysis containing 10 Randomised Controlled Trials and 1,863 patients demonstrated significant reduction in surgical site infections (58% reduction, $p<0.0001$), significant reduction in dehiscence (26% reduction, $p<0.01$) and significant reduction in length of stay (0.47 days reduction, $p<0.0001$)3. This summation of the evidence demonstrates the positive impact PICO is having on patient outcomes and system costs.

For our traditional NPWT system, RENASYS™, evidence was published demonstrating the effectiveness in the treatment of challenging wounds and its compatibility with ACTICOAT, where high bacterial burden is impacting wound progression4.

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

In 2017 performance in this franchise was led by PICO, which continued to perform strongly across the year.

1 These non-IFRS financial measures are explained and reconciled to the most directly comparable financial measure prepared in accordance with IFRS on pages 178–181.

2 Hurd, T., et al. Use of a portable, single use, negative pressure wound therapy device in home care patients with low to moderately exuding wounds. A case series. Ostomy Wound Management. March 2014. Vol.60. Issue 3.

3 V. Strugala & R. Martin, Meta-analysis of comparative trials evaluating a prophylactic single-use negative pressure wound therapy system for the prevention of surgical site complications. Surgical Infections (2017). DOI 10.1089/sur.2017.156.

4 Hurd, T., et al. A Retrospective Comparison of the Performance of Two Negative Pressure Wound Therapy Systems in the Management of Wounds of Mixed Etiology. Adv Wound Care (New Rochelle). 2017 Jan 1;6(1):33–37.

OUR RESOURCES

THE RESOURCES WE NEED TO DELIVER OUR PRODUCTS

OUR PEOPLE

Engaging, developing and retaining our more than 15,000 employees is important to us and we work hard to be a great place to work as well as a responsible corporate citizen.

SEE OPPOSITE

RESEARCH & DEVELOPMENT

Innovation is part of our culture and we invest 5% of our revenue to develop new products that will help to improve patients' lives.

PAGE 28

MANUFACTURING & QUALITY

We operate our global manufacturing efficiently, and to the highest possible standards, to ensure product quality at competitive pricing.

PAGE 29

SALES & MARKETING

We support our customers in over 100 countries. Our commercial teams are highly specialised with an in-depth knowledge across the full range of product franchises.

PAGE 30

ETHICS & COMPLIANCE

We are committed to doing business the right way and apply strict business principles to the way we deal with our customers and partners.

PAGE 32

TRAINING & EDUCATION

Every year, thousands of healthcare professionals attend our training courses around the world. Education is fundamental to how we support our customers.

OUR
PEOPLE

WE ARE PIONEERS WITH A PURPOSE

Smith & Nephew is a company of pioneers, extending access to advanced medical technologies and enabling better outcomes for patients globally. We've been doing this since 1856.

From our beginnings as a small family pharmacy in Hull, England, we have grown in size and scope. Over the past six years, we have fundamentally changed the structure of our Company, creating greater alignment and presenting one face to our customers. We have brought pioneering products and technologies to market, such as JOURNEY II and PICO, and have successfully completed many significant acquisitions, widening our customer base around the world.

We are proud of the work we do and share a mission to support healthcare professionals in their daily efforts to improve the lives of their patients. We achieve this by working together to deliver our strategic priorities.

Every employee has a role in our success, and so it is crucial that all employees feel engaged in their work and know its importance. We start each year by setting clear and measurable objectives based on our strategy scorecard.

The personal objectives of the Chief Executive Officer are cascaded through the organisation, with each employee setting aligned objectives according to his or her role.

Through this process, each employee can clearly see how their efforts contribute to the overall success of the business, which drives execution, accountability and engagement.

This engagement is measured through a biennial Global Employee Survey using the Great Place to Work Trust Index. In 2017, 88% of our global employees participated in this survey, providing meaningful results that have driven actions for improvement. We track our progress against these actions using regular pulse surveys.

In 2017 we raised our overall Trust Index score by five percentage points, to 67%, meeting our target for improvement. We achieved Great Place to Work recognition in a further five countries, ahead of our target of two more. In total we have received recognition in nine countries.

In addition to the Trust Index, we have implemented a culture dashboard which includes key metrics such as employee retention, business performance and feedback from new hires. The foundation of this dashboard is our values: to Perform, Innovate and Earn Trust. It provides a clear framework for our senior leaders to track progress and identify areas for additional focus, action or reinforcement.

CELEBRATING EXCELLENCE

The CEO Awards salute employees at all levels who make outstanding contributions for the benefit of Smith & Nephew.

In 2017 Lorraine Belleville, a Packaging Operator and Team Coordinator at our Mansfield facility in the US, was recognised for her significant contributions to Mansfield's improvement of 'Finished Goods' production by nearly 30% since 2016. Lorraine took initiatives to improve the flow of work at the facility by introducing important tools such as a tracking scheme, daily production sheet and visual management.

WE ENCOURAGE AND REWARD HIGH PERFORMANCE

We set ambitious targets and we achieve them by creating a sense of purpose and urgency. While achievement of these targets is crucial, our Performance Management Process measures not only what was achieved, but also that the behaviours displayed in doing so match our core values.

Smith & Nephew's compensation philosophy is to pay for performance. This means compensating employees for sustained performance that helps deliver timely and tangible results to drive the business forward. By following this philosophy we have found that we not only attract, retain, and motivate talent, but it also helps drive better business results and provides an equitable work environment. We are Living Wage Accredited in the UK, voluntarily paying above the government required minimum as we believe employees should receive fair compensation for the work they do.

The Company's 'Going the Extra Mile' global employee recognition programme is used by executives, managers and employees alike to recognise and reward performance and our corporate values.

We are committed to working with employees to develop each individual's talents, skills and abilities.

Employee advancement is merit-based, reflecting performance as well as demonstration of core competencies which include our values, with an emphasis on ethics and integrity. We prioritise the development and promotion of existing 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 well defined career development plans. The Board reviews succession plans for key executive roles and such plans are in place for other critical positions across our business.

In 2017, we added to our development programme three new opportunities: Leadership Edge, Pioneer and Continuous Learning Journeys. In 2017, 560 employees have participated in these programmes. These are designed to embed and enhance essential leadership skills for new and experienced managers, respectively through a combination of guided and self-service learning tools. Our 'myLearning' self-directed online learning portal was nominated for a Learning Technologies Award for the 'Best Online Distance Learning Programme' this year.

Employees are provided with opportunities to develop their skills and career through new assignments and on the job experiences.

BUILDING A LEADERSHIP CAREER

Laura Whitsitt has built a leadership career at Smith & Nephew.

Laura Whitsitt began her career at Smith & Nephew as an intern in product development. Thirty years later and now Senior Vice President of Research & Development for Orthopaedics, Laura says she still sees opportunities for growth and development. “I am often asked why I have stayed at the same company for so long. It’s important to me to learn and grow and be challenged, and I’ve always had those opportunities at Smith & Nephew.”

In the male-dominated industry of orthopaedics, Laura says she has always felt respected for her expertise. Among the highlights of her career is designing the

Company's first and only spinal systems and managing them through to successful launch.

Far from a barrier, Laura believes her perspective as a female leader has worked in her favour, and has added value. "As a woman I bring a different viewpoint to the table, and that's especially important in R&D," she says.

Laura says she has seen real progress over her career in adding more female leaders to the ranks at Smith & Nephew, but there is more to do. "Mentoring has been very valuable, and I have certainly seen a positive change in the number of females in managerial roles. The more diversity we have at higher levels of the Company, the more momentum we have to build on."

NUMBER OF EMPLOYEES1 2017		
15,933	59%	41%
Total employees	Male	Female
804	74%	26%
Senior managers2 and above	Male	Female
12	75%	25%
Board of directors	Male	Female

1 Number of employees at 31 December 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 and Directors of our subsidiary companies.

WE FOSTER AND EMBRACE DIVERSITY OF EXPERIENCE, BACKGROUND AND IDEAS

Smith & Nephew's global diversity and inclusion programme, called 'Valuing Difference', is designed to highlight the value of bringing different ideas and perspectives in from our work and personal experiences. Through storytelling and manager tools and discussion guides, the programme encourages open dialogue and an appreciation of the benefits of diverse teams.

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

When we recognise and appreciate these differences, they can help us better reflect the wide range of cultures, customers, and patients we serve, so we can better meet their needs and be a better business – thereby building credibility with all. Diversity is regarded as an asset and it is further guarded by our global policies regarding 'Diversity and Inclusion' and 'Respectful Workplace'.

Our Valuing Difference Programme is sponsored by Chief Executive Officer Olivier Bohuon, and Steering Committee members include our Chief Human Resources Officer, Members of the Executive Committee and Regional Presidents. Together, the committee agrees the strategy which is then executed at the regional and country-level in order to have the greatest possible impact.

Local diversity councils meet regularly and work to translate strategy to local needs, execute specific actions and share best practice.

An example of a Valuing Difference Initiative is the 'Elevate' programme, which was attended by more than 275 female professionals in 2017. Elevate is specifically designed to develop our female leaders and includes a mix of skill development and motivational support. The programme has been highly successful, with the majority of participants stating they prioritise making time to attend the monthly webinar sessions and more than one-third promoted or changed roles in the past year.

Gender diversity and equity are important areas of focus for us. Our goal is to have 33% women in senior management positions by 2020, in accordance with best practice as defined in the Hampton Alexander Report. Currently just over a quarter of senior management roles are held by women, in line with the FTSE100 average as defined by the 2017 Hampton Alexander Review. We are also committed to ensuring that our performance management and associated rewards are equitable and free from any unconscious gender bias. The UK government has introduced a requirement that all employers publish their gender pay ratio in the UK by 4 April 2018, which we will do on our website.

We recruit, employ and promote employees on the sole basis of the qualifications and abilities needed for the work to be performed. We do not tolerate discrimination on any grounds and provide equal opportunity based on merit. We do not use any form of forced, compulsory or child labour. We support the Universal Declaration of Human Rights of the United Nations. This means we respect the human rights, dignity and privacy of the individual and the right of employees to freedom of association, freedom of expression and the right to be heard. As a global medical technology

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

WE DO THE RIGHT THING EVEN WHEN NO ONE IS WATCHING

All employees receive our Code of Conduct and Business Principles when they join the Company, and renew their training and commitment to the Code on an annual basis.

Smith & Nephew's Global Compliance Programme not only helps our businesses comply with laws and regulations, but also creates the culture of trust we deem essential to our success. Our comprehensive programme includes: Board and executive oversight committees; global policies and procedures; on-boarding and annual training for employees and managers; training for third-party sellers; monitoring and auditing processes; and reporting channels and recognition for demonstrating our values. Annual training is required of all employees and any stakeholders who represent Smith & Nephew.

Through our global intranet, we provide resources and tools to guide employees to make decisions that comply with the law, local industry code and our Company Code of Conduct. We require advance approval for significant interactions with healthcare professionals or government officials and we regularly assess existing and emerging risks in the countries in which we operate. See page 32 for more information on our global compliance programme.

WE VIEW INNOVATION AS AN ESSENTIAL SKILL

Innovation is owned by all of us who question the status quo, dare to propose new solutions and seek to be the best at what we do for the benefit of our customers.

At Smith & Nephew, we recognise that innovation includes the entire value chain within our organisation from R&D to engineering, manufacturing, distribution, sales, marketing, and even facility utilisation and investment strategy. We also acknowledge only a few innovations will be truly disruptive, while others will result in equally as important incremental changes. To help aid this, Smith & Nephew has introduced an Innovation Council to support its culture of innovation and signal its importance in the Company's continued success.

The Council consists of 'Innovation Champions' who reflect the diversity of the Smith & Nephew employee base and have a strong appetite for trying new things. These champions will be responsible for generating creative ways to embed this value and look for opportunities to raise innovative opportunities to the leadership team and to celebrate success.

WE CARE ABOUT EACH OTHER'S WELLBEING AND THE SUSTAINABILITY OF SMITH & NEPHEW

Each of us treats our Company's resources and the world's natural resources as if they were our own, and we take our responsibility to our communities seriously. Smith & Nephew not only applauds, but also supports the donations of employees' time and resources.

We encourage all our employees to volunteer their time and talents by providing eight hours per year paid time for volunteer efforts. Many functions structure their team building activities around group volunteering opportunities such as Make a Wish Foundation events and the Helping Hands Project which builds prosthetic hands for amputees in third-world countries.

Charity efforts are also coordinated across entire sites, and beyond. In 2017, Smith & Nephew brought together many local companies in Hull with a 'More Together' initiative to raise tens of thousands of pounds for local charities. Smith & Nephew was also a major sponsor of the Hull City of Culture celebrations, with employees contributing to and benefiting from the year of activities on-site and across the city.

Our social responsibility strategy is to materially contribute to the delivery of our Company Mission by engaging employees to prioritise philanthropic resources and efforts on areas that align with our business strategy and values. Resources include product donations, matching gifts, and employee volunteerism.

We believe selection and management of charitable and non-profit organisations and activities is best accomplished at the local level within the framework of our social responsibility strategy. Each location's Site Leadership Council and/or Camaraderie Council will design, construct, and operate the local programme, including arrangement of funding. These Councils build out the local social responsibility programme, selecting charitable organisations and activities that best engage the local employee population and underpin our Mission.

We Innovate.

We Perform.

We earn Trust.

We are Smith & Nephew.

RESEARCH & DEVELOPMENT (R&D)

$223m
Investment
in R&D in
2017

Smith & Nephew has a single global R&D function, led by the President of Global R&D, reporting directly to the Chief Executive Officer. This team strives to increase value created by research and development by focusing on three imperatives: Disruptive Innovation that matters, flawless execution of new product development, and compelling evidence of clinical and economic value.

The Portfolio Innovation Board drives our innovation strategy and framework. This Board identifies and selects only those projects that will make a meaningful difference to our customers and their patients. This includes continuing to invest in incremental innovation to improve existing products in a way that improves outcomes. It also involves driving greater efficiency through innovation, potentially reducing our costs of goods. For instance, by making instrument sets more procedure and patient-specific, we will reduce complexity and cost, to the benefit of customers and the Company. Finally, by seeking more meaningfully disruptive products and services, we will harness transformational innovation to provide access to new technologies to people across the world.

Second, the team challenges itself to execute flawlessly. This means developing the right product at the right cost and quality, supported by clinical evidence, in a timely manner. 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 fulfil an unmet clinical need, have a strong commercial rationale, and are technologically feasible. The R&D function works closely with the marketing, clinical, regulatory affairs, manufacturing and supply chain management teams to ensure we can produce new products to clinical, cost and time specifications.

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

During 2017 we secured a long-term partnership with the University of Hull to create one of the world’s largest Wound Care Research Clusters with the aim of developing scientific insights and innovative treatments. This includes the creation of eight PhD studentships and a programme of collaboration between Smith & Nephew’s new Hull R&D centre and the University’s new Health Campus, both of which opened in 2017.

We also announced a three-year partnership with Imperial College London to develop enhanced surgical techniques relating to ligament function, biomechanics and soft tissue injuries of the knee, including the most common injuries of torn menisci and anterior cruciate ligament rupture. See opposite page.

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

In 2017, we invested $223 million in R&D, in line with our commitment, set out in 2011, to maintain our investment level at around 5% of revenue. We expect to maintain this proportion going forward, but to realise greater benefit through our new structure and strategic focus.

INNOVATING THROUGH PARTNERSHIP

Smith & Nephew is working with Imperial College London to develop enhanced surgical techniques relating to ligament function, biomechanics and soft tissue injuries of the knee, including the most common injuries of torn menisci and anterior cruciate ligament rupture.

“The partnership with Smith & Nephew is priceless for our work. It allows a strategic attack on the unanswered biomechanical issues in knee surgery. Knowing funding is secure for three years allows a step-by-step ‘due diligence’

approach to investigating these issues rather than sporadic studies. This is the best way to translate from the lab to patient care" said Mr Andy Williams, Lead Surgical Researcher, Imperial College London and Fortius Clinic.

Meniscus repair is one of the greatest challenges of Sports Medicine. By combining the clinical expertise of Imperial College with our pioneering approach to new product development we expect to be able both to advance surgical techniques and accelerate the development of next generation products.

MANUFACTURING & QUALITY

GLOBAL OPERATIONS

Smith & Nephew takes great pride in its expertise in manufacturing products to the highest quality and ensuring they reach our customers in a timely manner. We operate manufacturing facilities in a number of countries across the globe, and a number of central distribution facilities in key geographical areas. Products are shipped to individual country locations which hold small amounts of inventory locally for immediate supply to meet customer requirements.

Manufacturing is a dynamic process and our Global Operation leadership team is focused on successfully supporting delivery of the Group's strategic priorities by ensuring our footprint and expertise is ready to respond to geographical

growth, new product development, greater external regulatory scrutiny and the commercial pressure to be ever more efficient.

Quality has always been paramount to Smith & Nephew. We have a unified Quality Assurance and Regulatory Affairs team to ensure consistency across our country business units. Requirements of global regulatory agencies have become more stringent in recent years and we expect them to continue to do so. We are continuing to expand our portfolio globally through new product development and by registering our existing products in new markets. In order to meet the expectations of regulators and support this added complexity we continued to invest in our Quality and Regulatory expertise in 2017.

OUR MANUFACTURING FACILITIES

Our largest manufacturing operation is based in Memphis (Tennessee, US). The Memphis facilities produce key products and instrumentation in our Knee Implant, Hip Implant and Trauma franchises. These include the JOURNEY II and LEGION knees, the ANTHOLOGY Primary Hip System and key Trauma products such as the PERI-LOC Plating System, REDAPT and TRIGEN Intramedullary Nails. In addition to this, Memphis is home to the design and manufacturing process of the VISIONAIRE patient matched instrumentation sets, and OXINIUM™ Oxidised Zirconium. This patented metal alloy is available for many of our knee and hip implant systems as part of our VERILAST technology.

In Sports Medicine, our Alajuela (Costa Rica) facility, opened in 2016, manufactures COBLATION technology. Our Mansfield (Massachusetts, US) facility manufactures 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 HEALICOIL PK suture anchor.

The Aarau (Switzerland), Tuttlingen (Germany), Beijing (China) and Devrukh (India) facilities manufacture a number of surgical device products including key reconstruction and trauma products and the PLUS™ knee and hip range. The Warwick (UK) facility produces the BIRMINGHAM™ Hip Resurfacing System.

Our Oklahoma City (Oklahoma, US) facility produces and services electro/mechanical capital equipment as well as single use sterile devices and also assembles some of our NPWT devices using components from third parties.

The majority of our wound management products are manufactured at our facilities in Hull, Suzhou and Curaçao. These include pioneering products such as PICO and ALLEVYN Life as well as our complex silver coating technology for ACTICOAT. In Suzhou, we also manufacture our wound care products for the mid-tier in the Emerging Markets. Manufacturing of our Advanced Wound Bioactive products takes place in Curaçao and at various third party facilities in the US.

PROCUREMENT

We procure raw materials, components, finished products and packaging materials from suppliers in various countries. These purchases include metal forgings and castings for orthopaedic products, optical and electronic sub-components for sports medicine products, active ingredients and semi-finished goods for Advanced Wound Management as well as packaging materials across all product ranges.

Suppliers are selected, and standardised contracts negotiated, by a centralised procurement team wherever possible, with a view to ensuring value for money based on the total spend across the Group. On an ongoing basis, we work closely with our key suppliers to ensure high quality, delivery performance and continuity of supply.

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

GLOBAL SUPPLY CHAIN

Our Global Supply Chain function ensures that our products reach our internal and external customers where and when they are needed, in a compliant and efficient manner. Bringing together people, knowledge and expertise helps us meet our objectives and our customers' expectations, driving us to become more competitive, responsive and integrated.

We operate three main holding warehouses for surgical products, one in each of Memphis, Baar (Switzerland) and Singapore. These facilities consolidate and ship to local country and distributor facilities. Our distribution hubs for advanced wound products are located in Neunkirchen (Germany), Derby (UK) and Lawrenceville (Georgia, US).

SALES &
MARKETING

Our customers are the providers of medical and surgical treatments and services in over 100 countries worldwide, ranging from orthopaedic surgeons to wound care nurses, general practitioners and other clinicians, but increasingly also economic stakeholders. These include purchasing professionals in hospitals, healthcare insurers, materials managers and others.

We serve these customers through our sales force and other channels. Our sales representatives are highly trained and skilled individuals. Becoming a sales representative requires intense training, including passing a strict certification programme. Depending on their area of specialism, representatives in our surgical businesses must be able to demonstrate a detailed knowledge of all the surgical instruments used to implant a device, or have specific understanding of the various surgical techniques a customer might use. In our advanced wound management business, sales representatives must have a detailed understanding of how patients live with wounds and how clinicians seek to prevent and treat them, as well as deep knowledge of the clinical and economic benefits of using our products within treatment protocols.

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

Our Global Commercial Organisation oversees all commercial activities (sales, marketing, market access, and commercial strategy) across the Group for our full line of business. The organisation is led by two regional sales presidents for the US and International, and our Chief Marketing Officer (CMO). Within our International region there are several regional leaders for Europe & Canada, Asia Pacific and Latin America.

Our sales forces in the Established Markets are specialised by channel and consist of a mixture of independent contract workers and employees. In our Emerging Markets we operate through direct selling and marketing operations led by country managing directors, and through third party sellers.

Smith & Nephew has three global marketing teams who set the strategic direction of our businesses, guide our research & development teams by specifying new products & services needed to realise those strategies, and develop the promotional assets and guidance to commercialise our products. They utilise a variety of traditional and novel means to market to our customers, including scientific congresses, commercial trade shows, advertising in medical journals and, increasingly, digital channels. These include product websites, social media channels, mobile applications and our professional educational platform called Education & Evidence.

Also reporting to our CMO is the global Commercial Excellence team, which drives numerous initiatives to strengthen commercial execution in both the sales organisation and our global marketing teams. There is a strong focus on Sales Force Excellence to increase efficiency and effectiveness of our sales teams, and on Pricing to increase discipline in our transactional pricing and define better value creation strategies for our innovative products. Other activities in Commercial Excellence include strategic planning, business intelligence and market research, digital marketing, and marketing communications.

In addition, our Health Economics and Outcomes Research (HEOR) team generates evidence on the economic impact of our products and provides supporting assets and tools to commercialise our products. They do this through collaboration with leading medical centres in the world as well as existing registries that track usage of our products. The HEOR team also reports to our CMO.

A DAY IN THE LIFE…

Mustafa works as a Territory Manager in our Sports Medicine franchise in the UK.

“Every day is different. My time is split between supporting customers and their operating theatre teams in hospitals, meeting with potential customers, learning and researching techniques and trends, and keeping in touch with my colleagues, the business and my existing customers.

“My favourite part of the job is the interactions I have with my customers. I believe that we sell solutions rather than products, so everything I do is about helping my customers to find answers to the problems they face, to enable better outcomes for their patients.

“We’re very lucky in the UK to be able to offer an excellent training facility to the surgeons we support. It’s a great feeling to be able to support a consultant to refine their surgical techniques. I’m also a mentor providing expertise and guidance on our Resection and Camera products to my colleagues in the UK.”

ETHICS & COMPLIANCE

CODE OF CONDUCT AND BUSINESS PRINCIPLES

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

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

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

GLOBAL COMPLIANCE PROGRAMME: EXISTING ELEMENTS

Smith & Nephew has implemented what we believe to be a world-class Global Compliance Programme that helps our businesses comply with laws and regulations. This comprehensive compliance programme includes: Board and executive oversight committees; global policies and procedures; on-boarding and annual training for employees and managers; training for distributors and agents and higher-risk vendors; monitoring and auditing processes; reporting channels and employee-recognition for demonstrating our values in their everyday work.

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

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

New distributors and other higher-risk third parties are subject to screening and are contractually obligated to comply with applicable laws and our Code of Conduct. Compliance training and certifications are included in this process.

Managing Directors are required to complete an annual certification to the Chief Executive Officer to confirm the implementation of required policies. Managers and employees make an annual compliance certification and conflict of interest disclosure. Executive management, managers and employees have a compliance performance objective

customised to their role.

GLOBAL COMPLIANCE PROGRAMME: NEW ELEMENTS IN 2017

In 2017, we created an Ethical Leadership model, which includes four pillars: Advise, Lead, Observe, and Coach or Report. We introduced this model during annual manager training, reinforced the model through further communications, and gave managers resources they can use to raise awareness of compliance risks and rules.

We benchmarked our whistle-blower programme against industry metrics. The benchmarking confirmed that all Smith & Nephew reporting and substantiation rates met industry practices. We conducted a comprehensive review of the guidelines recently issued by the US Department of Justice on compliance programme effectiveness and by the International Organisation of Standards on Anti-Bribery Management Systems, and are also identifying any actions needed to align to this new guidance.

We applied enhanced standards prospectively for new, potential partners and retrospectively for existing distributors. We also developed new guidelines for distributors or agents who need to enter the operating room when acting on our behalf. We worked with our Procurement colleagues to integrate compliance controls into the Company's new purchasing system. We also conducted a comprehensive review of the types of complementary workers we engage to ensure they receive appropriate anti-bribery and corruption compliance training and will implement an updated training strategy in 2018.

TRAINING & EDUCATION

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

In February 2017, we inaugurated our 'Expert Connect Centre' in the UK. This new centre for HCP training is a state-of-the-art learning environment with the latest audio-visual capabilities and 14 station bio-skills laboratory for all levels of HCPs from around the globe. In 2017, we provided more than 45,000 instances of training to surgeons through our Smith & Nephew training centres in the US, UK and China, as well as running many courses at third party centres around the world.

Working under expert guidance, attendees learn new techniques and refine skills, to ensure the safe and effective use of our products.

These courses are attended by residents, fellows and practicing surgeons who work together to review, discuss and train on current and forward-looking surgical techniques in their areas of clinical expertise. Our courses help up-and-coming surgeons develop trust and gain the experience and confidence necessary to become experts in their field.

Thousands of nurses receive face-to-face training from Smith & Nephew representatives every year, including attending courses at our centres, and through our representatives visiting them at their place of work. In 2017 almost 45,000 clinicians in the US alone benefited from our wound care educational resources.

In addition, we provide healthcare professionals our online resources such as the Global Wound Academy, The Wound Institute and, for surgeons, our Education and Evidence website. Recently we began utilising innovative, digital technologies to accelerate the learning experience of surgeons. In 2017 we doubled the number of healthcare professionals trained digitally on Smith & Nephew products and techniques to 180,000.

SUSTAINABILITY

SUSTAINABILITY IS BETTER BUSINESS

TAKING SUSTAINABILITY TO THE CORE OF THE BUSINESS

We began to deliver in 2017 our commitment to sustainability embodied in our refreshed Group Sustainability Strategy. This strategy, approved in 2016, both drives and is driven by implementation of the Group Business Strategy, ensuring that all three main aspects of sustainability – economic prosperity, social responsibility and environmental stewardship – advance as one.

This is a summary report of our sustainability activities and progress in 2017. Our annual Sustainability Report, published at the same time as this Annual Report, describes the Group Sustainability Strategy and its associated goals in more detail. It also specifies targets to move our performance towards these goals, and provides further information regarding our 2017 progress. It is available on our website.

GROUP SUSTAINABILITY STRATEGY

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

Sustainability is a journey, and in 2016 we thought deeply about our destination for the longer-term. The result was a new Group Sustainability Strategy. At the heart of this are ten long-term aspirational goals. These encompass all aspects of our business, and will inform and drive our business strategy for years to come. The Board has endorsed these and executive management is behind them. These goals are set out overleaf.

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

Longer term goals need medium-term SMART (specific, measurable, achievable, realistic and timebound) targets to ensure we are making the right progress. And we have taken such targets through 2020. These targets are discussed in more detail in the 2017 Sustainability Report which is available on our website.

2017 was a year in which our refreshed sustainability strategy was put into action. We delivered improvements across our traditional areas of focus: employee health and safety, carbon emissions and water consumption. In addition, we began to get a fuller understanding of our impacts in the areas of material efficiency, life cycle environmental impacts, and labour practices. We adopted a social responsibility strategy which will drive employee engagement and improve the communities in which we operate.

EMPLOYEE SAFETY, WELLNESS AND VOLUNTEERING

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

Engagement with the communities in which we operate continued to broaden and deepen through the active attention of site leadership, establishment and empowerment of local camaraderie councils, broader application of company-paid volunteering allowance, and increase in the company match for employee donations to charity. We continue to strengthen and deepen employee wellness programmes with a focus on enabling healthy lifestyle choices.

SOCIAL RESPONSIBILITY STRATEGY IMPLEMENTATION

In 2017, we developed and adopted a social responsibility strategy aimed at improving the alignment of our charitable donation, volunteering, wellness and professional development with both our Group Business Strategy and the needs and desires of our employees. The aim is to positively impact both employee engagement and the quality of life in communities in which we operate. We have improved our understanding of compliance to labour standards in our value chain, product and service attributes which are important to customers and our employees' view of the role of the organisation in society. In 2018, we will use these and other social success factors, informed by our Group Business Strategy as well as our Company values, to deploy a series of platforms and actions which advance our cause.

SUSTAINABILITY VISION AND MISSION

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

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

– Satisfy unmet health needs and promote greater access to treatment;

– Offer easier, better, faster and more effective treatment, enabling productive engagement in society;

– Prioritise materials that are reused, remanufactured, or recycled;

– Are manufactured using raw materials sourced from an environmentally and socially sound supply chain;

– Use natural resources efficiently;

– Are manufactured by processes that are not hazardous to people or the environment; and

– Implement the most sustainable product options.

Our plan focuses on both the foundational and competitive advantage elements required to deliver our value proposition sustainably. We employ a continuous improvement approach based upon the implementation of forward-looking solutions (such as investing in new materials and processes that provide significant benefits with respect to human rights, safety, energy, waste and/or communities) and bridging technologies to secure future game-changing performance.

OUR PERFORMANCE IN 2017

Our 10 long-term aspirational goals	2020 targets	Progress since 2016
1 Zero work-related injuries and illnesses across the value chain.	– 10% reduction in Total Injury Rate (TIR) from 2016 actual.	– In 2016 the TIR = 0.52, in 2017 TIR = 0.35 (33% lower).
2 Water: Total water impacts of our products and solutions are balanced with local human and ecosystem needs.	– Water footprint (1) available for products accounting for 75% of revenue and (2) considerations embedded in new product development process. – Total potable water consumption at S&N sites no higher than 2016 actual.	– Products accounting for 75% of revenue identified. Water footprint tools identified. – Work plan under development, will be approved and commenced in 2018. – Water reduction of 10%.
3 Waste: All materials are either shipped as part of product or returned for beneficial use.	– Total material efficiency estimated for products accounting for 75% of revenue – 80% or more of waste generated reused, recycled or recovered.	– Products accounting for 75% of revenue identified. Material efficiency tools identified. – Work plan under development, will be approved and commenced in 2018. – We currently reuse, recycle or recover energy from 77% of our total waste, up from 74% in 2016.
4 Carbon: 80% absolute reduction in total life cycle greenhouse gas emissions by 2050.	– Estimate total life cycle greenhouse gas emissions of products accounting for 75% of revenue. – Total Scope 1 & 2 greenhouse gas emissions reduced by 10% from 2016 actual.	– Products accounting for 75% of revenue identified. Total lifecycle greenhouse gas emissions tools identified. – Work plan under development, will be approved and commenced in 2018.

			– In 2017 the reduction is 7%.
5	Ethical Business Practices: All activities are conducted in compliance with applicable International Labour Organization (ILO) conventions, involve no environmental degradation, and are free from corruption.	– Labour practices throughout the supply chain associated with products accounting for 75% of revenue compliant with applicable ILO conventions.	– Products accounting for 75% of revenue identified. Gap assessment to applicable ILO conventions completed for internal operations. Engagement with upstream suppliers and downstream distributors and agents ramping up.
6	Zero Product-related and service-related patient injuries.	– Robust system in place to detect, record, investigate and eliminate root cause of product-related and service-related patient injuries.	– Systems are in place to detect, record and investigate patient injury incidents. Patterns in the data are being used to craft models which will allow identification of at-risk attributes.
7	Robust social responsibility programmes that contribute to the attraction and retention of top talent.	– Social responsibility strategy which aligns philanthropy, employee volunteering and wellness to the business strategy in place.	– Social responsibility strategy in place. Alignment of current initiatives to the strategy under way.
8	Products and services are aligned to market economic, social and environmental expectations and anticipate future market conditions: – All products have identified and clearly-described sustainability attributes. – R&D and NPD processes deliver environmental-, social-, and healthcare economically-advantaged innovations.	– Sustainability attributes described for products accounting for 75% of revenue Robust emphasis on sustainability attributes of new products/services in place.	– Products accounting for 75% of revenue identified. Product/service sustainability attributes agreed. – New product development (NPD) sustainability focus planning under way.
9	Strategic risks and opportunities are understood and business activities are aligned to risk appetite.	– Enterprise risk management arrangements are embedded in the routine business decision-making process.	– Risk register reinvigorated. Deep dive programme instituted with focus on both assurance that all relevant risks have been identified and effectiveness of mitigating actions is accurately assessed. – Actions to further embed into the business decision-making process are planned for 2018.
10	Environmental, social, and economic impacts of (1) potential acquisitions, (2) technologies to be extended to Emerging Markets, (3) innovative business models, (4) cost-of-quality reduction initiatives, and (5) manufacturing siting, functional optimisation and site utilisation alternatives	– Formal programmes in place to measure/assess the economic, social and environmental impacts of (1) potential acquisitions, (2) technologies to be extended to Emerging Markets, (3) innovative business models, (4) cost-of-quality	– Launched our Enterprise Risk Management Policy and Manual. – Trained our risk champions in risk identification and mitigation.

are fully understood and appropriately balanced.	reduction initiatives, and (5) manufacturing siting, functional optimisation and site utilisation alternatives.	– Introduced a product focused approach to risk management. – Conducted a number of 'deep dives' into several key risks. – Tools and standards to address new technologies are being developed to support our NPD work above.

These targets are discussed in more detail in our 2017 Sustainability Report which is available on our website.

CO_2e REPORTING

	2017	2016	2015
CO_2e emissions (tonnes) from:			
Direct emissions	9,451	9,822	11,011
Indirect emissions	76,107	82,415	77,191
Total	85,558	92,237	88,202
Intensity ratio			
CO_2e (t) per $m sales revenue	17.8	19.6	19.2
CO_2e (t) per full-time employee	5.2	5.9	6.0

Revenue: 2017: $4.8bn; 2016: $4.7bn; 2015: $4.6bn.
Full-time employee data: 2017: 16,333; 2016: 15,584; 2015: 14,686.

Notes

2015 data adjusted to exclude acquisitions in Russia and Colombia.
2017 data includes all data, including acquisitions since 2016.

CO_2e reporting methodology, materiality and scope.

We report the carbon footprint of our Scope 1 and 2 greenhouse gas (GHG) emissions in tonnes of CO_2 equivalent from our business operations for the calendar year ended 31 December 2017. Our focus is on the areas of largest environmental impact including manufacturing sites, warehouses, R&D sites and offices. Smaller locations representing less than 2% of our overall emissions are not included. Acquisitions completed before 2017 are included in the data, with more recent ones being excluded and this is in line with our established policy for integration of acquired assets. Each year we work with an independent partner to verify our sustainability data and gain assurance.

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

We report our emissions in two ‘scopes’.

Scope 1 figures include: Direct sources of emissions mainly comprise the fuels we use on-site, such as gas and heating oil and fugitive emissions arising mainly from the losses of refrigerant gases.

Scope 2 figures include: Indirect sources of emissions such as purchased electricity and steam we use at our sites.

Location-based emissions are calculated in compliance with the WRI/WBCSD GHG Protocol Corporate Accounting and Reporting Standard and have been calculated using carbon conversion factors published by BEIS/DEFRA for 2017. We have applied the emission factors most relevant to the source data, including DEFRA 2017 (for UK locations), IEA 2015 (for overseas locations) and for the US we have used the US EPA ‘Emissions & Generation

Resource Integrated Database' (eGrid) for the regions in which we operate. All other emission factors for gas, oil, steam and fugitive emissions are taken from DEFRA, 2017.

GETTING SERIOUS ABOUT SOLAR

In line with our aspiration to reduce carbon emissions, we are investing in more efficient energy solutions, such as solar power.

Devrukh, India

At our Devrukh site in India, we are running one of our largest renewable energy projects.

By installing the 426 kVA roof top solar panel system, we aim to produce enough energy to provide the site with free power for 25 years, whilst reducing carbon emissions by up to 44% per annum. We are already achieving a

cost saving of 44% per year and expect a return on investment in less than five years.

The 1,330 solar panels will also enable us to reduce the inside temperature of the manufacturing floor by five to ten degrees celsius, creating a safer and more pleasant working environment for our employees.

Suzhou, China

In April 2017, we installed 24 sets of solar water heater units on the roof of one of our buildings in Suzhou. The system can produce around 12 tonnes of 55˚C hot water every day for the site's hot water system and will save 291 tonnes of steam every year.

CHIEF FINANCIAL OFFICER'S REVIEW

BUILDING A MORE

COMPETITIVE

BUSINESS

I am excited by the prospects for 2018 and beyond as we realise the opportunities in front of us.

DEAR SHAREHOLDER

I am delighted to address you for the first time in the Annual Report as your Chief Financial Officer.

Under Olivier's leadership, Smith & Nephew has made significant organisational changes to create a strong global business. I believe that we are just starting to see the benefits of these changes, and I am excited by the prospects for 2018 and beyond as we realise the opportunities in front of us. I am very much looking forward to working with Olivier and, in due course, his successor, to make this happen.

2017 PERFORMANCE

Group revenue in 2017 was $4,765 million, an increase of 2% on a reported basis and 3% on an underlying basis1. This was an improvement from underlying growth of 2% in 2016. Trading profit1 was $1,048 million, and the trading profit margin1 was 22.0%, up 20bps on 2016. I am pleased to report that both our underlying revenue growth and trading profit margin improvements were in-line with our guidance.

The reported operating profit for 2017 was $934 million, up from $801 million in 2016, with the year-on-year increase primarily reflecting a gain of $54 million from the settlement of an intellectual property matter, no restructuring charges and lower amortisation and impairment of acquisition intangibles in 2017.

The tax rate on trading results1 was 17.1% (2016: 23.8%). This is a considerable reduction on the 2016 rate and is mainly due to a one-off benefit following the conclusion of a US tax audit, further progress in improving our tax rate, tax provision releases following expiry of statute of limitations and a beneficial geographical mix of profits. The reported tax rate of 12.7% was a result of the lower tax rate on trading results and also included a $32 million net benefit from US tax reform.

Adjusted earnings per share1 (EPSA) was up 14% at 94.5¢ as a result, and this is reflected in the 14% increase in our full year dividend distribution for 2017. Basic earnings per share (EPS) was 87.8¢ in line with the previous year.

I am pleased to report that trading cash flow1 was $940 million, up from $765 million in 2016, with a higher trading profit to cash conversion ratio1 of 90% as we improved our working capital management.

As the result of improved operating profit, the lower tax rate and a stable asset base we saw an improvement in Return On Invested Capital1 (ROIC-as defined on page 39) from 11.5% in 2016 to 14.3% in 2017.

CAPITAL RETURNS

The appropriate use of capital on behalf of shareholders is important to Smith & Nephew. The Board believes in maintaining an efficient, but prudent, capital structure, while retaining the flexibility to make value-enhancing acquisitions.

This approach is set out in our Capital Allocation Framework which we used to prioritise the use of cash and ensure an appropriate capital structure.

Our commitment, in order of priority, is to:

– Continue to invest in the business to drive organic growth;

– Maintain our progressive dividend policy;

– Realise acquisitions in-line with strategy; and

– Return any excess capital to shareholders.

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

IMPROVING COMPETITIVENESS

On joining Smith & Nephew I was asked by Olivier and the Board to look afresh at efficiency opportunities within our business. Some preliminary analysis highlighted a number of areas of opportunity, and we conducted a detailed assessment of these during the final months of 2017.

Our conclusion was that we now have the Group structure in place which lets us act on these further opportunities. Through better execution and efficiency we can and will strengthen our competitive position.

We are calling this work the APEX programme, standing for ‘Accelerating Performance and Execution’, and we completed our planning and started to take action in early 2018. Our three workstreams are focused on clear and obtainable improvements in the Group’s manufacturing, warehousing and distribution footprint, reducing our general and administrative expenses, and driving greater commercial effectiveness. More details on APEX and each of these workstreams can be found on page 14.

APEX is expected to deliver an annualised benefit of $160 million by 2022, with at least half of this expected by 2020, for a one-off cash cost of up to $240 million.

SUCCESSFUL ACQUISITION

During the year, we continued to seek further opportunities to strengthen our technology and product portfolio. In December we acquired Rotation Medical, Inc., the developer of a novel tissue regeneration technology for shoulder rotator cuff repair, for an initial cash consideration of $125 million and up to a further $85 million over the next five years, contingent on financial performance. I am excited by the potential for this new technology and we remain alert to further opportunities to bring other disruptive innovations into the Group.

OUTLOOK

We expect the overall dynamics in our markets to be similar in 2018 to those seen in 2017. Against this backdrop, the Group expects to continue to deliver an improved performance in 2018 driven by our by our strong product portfolio and pipeline of innovative products.

In terms of revenue, we expect our underlying growth to be in the range of 3% to 4% (which equates to 7% to 8% in reported terms at exchange rates prevailing on 2 February 2018). In terms of trading profit margin we expect to drive a further 30 70bps improvement over 2017. As a result of the recently enacted US tax reform, we expect a tax rate on trading results in the range 20% to 21%, barring any changes to tax legislation or other one-off items.

In 2018, we will continue to push for further success as we build a more competitive Smith & Nephew. I look forward to helping to drive this, and to delivering on our commitments for the benefit of all of our stakeholders.

Yours sincerely,

Graham Baker
Chief Financial Officer

FINANCIAL HIGHLIGHTS

$4,765m	
Revenue	
+2%	+3%
Reported	Underlying1
87.8¢	0%
Earnings per share EPS	
94.5¢	+14%
Adjusted earnings per share (EPSA)1	

1 These non-IFRS financial measures are explained and reconciled to the most directly comparable financial measure prepared in accordance with IFRS on pages 178–181.

FINANCIAL REVIEW

DELIVERING ON OUR COMMITMENTS

GROUP PERFORMANCE

HIGHLIGHTS FOR THE YEAR ENDED 31 DECEMBER

	2017	2016	Change
	$ million	$ million	$ million
Consolidated income statement			
Revenue	4,765	4,669	96
Operating profit	934	801	133
Trading profit1	1,048	1,020	28
Profit before tax	879	1,062	(183)
Attributable profit	767	784	(17)
EPS	87.8¢	88.1¢	(0.3¢)
EPSA1	94.5¢	82.6¢	11.9¢
Consolidated balance sheet			
Goodwill and intangible assets	3,742	3,599	143
Other non-current assets	1,393	1,216	177
Current assets	2,731	2,529	202
Total assets	7,866	7,344	522
Total equity	4,644	3,958	686
Non-current liabilities	1,876	2,038	(162)
Current liabilities	1,346	1,348	(2)
Total liabilities	3,222	3,386	(164)
Total liabilities and equity	7,866	7,344	522
Net debt1	1,281	1,550	(269)
Consolidated cash flow statement			
Cash flows from operating activities	1,273	1,035	238
Trading cash flow1	940	765	175
Free cash flow1	714	457	257

NON-IFRS MEASURES

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

	2017 $ million	2016 $ million	Reported growth %	Underlying growth %	Reconciling items Acquisitions/ Disposals %	Currency impact %
US	2,306	2,299	0%	2%	(2%)	0%
Other Established Markets	1,678	1,679	0%	0%	0%	0%
Emerging Markets	781	691	13%	12%	0%	1%
Total	4,765	4,669	2%	3%	(1%)	0%

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

	2017 $ million	2017%	2016 $ million	2016%
Operating profit	934	19.6%	801	17.2%
Acquisition-related costs	(10)	(0.2%)	9	0.2%
Restructuring and rationalisation costs	–	–	62	1.3%
Amortisation and impairment of acquisition intangibles	140	2.9%	178	3.8%
Legal and other	(16)	(0.3%)	(30)	(0.7%)
Trading profit	1,048	22.0%	1,020	21.8%

RESULTS OF OPERATIONS

In 2017, we delivered reported revenue growth of 2% and underlying revenue growth1 of 3%. Revenue growth on a reported basis was flat across our US and other Established Markets, with a strong performance in Japan driven by Sports Medicine and Knee Implants counterbalanced by a soft wound care market in the UK where we have now taken steps to adapt our business in response.

In our Emerging Markets reported revenue growth was 13% and underlying growth1 was 12% in 2017. In China, our largest Emerging Markets country, we delivered double-digit revenue growth as we improved our channel management. In the oil-dependent Gulf States we returned to growth by focusing on securing more private healthcare business to compensate for the reduction in government tenders. We are well positioned to continue to drive strong growth from the Emerging Markets over the medium term.

Operating profit of $934 million (2016: $801 million) is after integration and acquisition costs, as well as amortisation and impairment of acquisition intangibles and legal and other items. The year-on-year increase in operating profit primarily reflects a gain of $54 million from the settlement of an intellectual property matter, no restructuring charges and lower amortisation and impairment of acquisition intangibles in 2017. The sale of the rights to distribute certain non-core products contributed $19m to operating profit in 2017. In 2016 similar product disposals along with provision releases from favourable legal matter outcomes contributed $18m.

Trading profit1 was $1,048 million (2016: $1,020 million). Trading profit margin1 was 22.0%, up 20bps year-on-year, in line with guidance.

In 2017, selling, general and administrative expenses included a $10 million credit relating to acquisition-related costs (2016: $9 million charge), $16 million credit for legal and other costs primarily related to the settlement of patent litigation (2016: $30 million credit for legal and other primarily related to a $44 million curtailment credit related on

UK post-retirement benefits) and $140 million charge for amortisation and impairment of acquisition intangibles (2016: $178 million charge).

Research and development expenditure as a percentage of revenue remained broadly consistent at 4.7% (2016: 4.9%) with expenditure of $223 million in 2017 compared to $230 million in 2016.

Profit before tax in 2016 includes the $326 million profit on disposal of the Gynaecology business.

The Group has completed its review of the new US tax reform legislation, as enacted in December 2017, including the reduction of the US federal tax rate from 35% to 21%, which came into effect on 1 January 2018. As a result, the Group expects a positive impact on its tax charge for future years in addition to the one-off tax benefit in 2017 as discussed below. Parts of the new legislation are subject to questions of interpretation, and further regulations may be issued in the future to clarify or change certain elements, which may affect future tax charges.

Included in the total tax charge is a $32 million net benefit as a result of US tax reform legislation which comprises a benefit from a revaluation of deferred tax balances included within changes in tax rates, partially offset by a current tax charge relating to the deemed repatriation of foreign profits not previously taxed in the US.

Our reported tax rate of 12.7% (2016: 26.2%) has decreased due to the $32 million net benefit in 2017 from US tax reform, the lower tax rate on trading results and the impact of the Gynaecology disposal in 2016. Our trading tax rate1 is 17.1% (2016: 23.8%) with the reduction due to a one-off benefit following the conclusion of a US tax audit, further progress in improving our tax rate, tax provision releases following expiry of statute of limitations and a beneficial geographical mix of profits.

BALANCE SHEET

Goodwill increased by $183 million as a result of $132 million arising on the acquisition of Rotation Medical, Inc. and favourable currency movements of $51 million. Intangible assets decreased by $40 million with net movements relating to additions, disposals and transfers of $70 million relating to intellectual property, distribution rights and software acquired together with $61 million recognised with the acquisition of Rotation Medical, Inc. Amortisation and impairment during 2017 was $202 million and there were favourable currency movements of $31 million.

Other non-current assets increased by $177 million primarily due to a $67 million increase in property, plant and equipment with additions offsetting depreciation, and the recognition of retirement benefit assets of $62 million for our UK and US pension schemes. Current assets increased by $202 million with trade and other receivables increasing $73 million primarily due to $45 million of foreign exchange, inventories increasing $60 million primarily due to foreign exchange and cash increasing $69 million due to the timing of receipts.

Non-current liabilities decreased by $162 million primarily due to payments made against our borrowing facilities. Current liabilities decreased by $2 million as a $73 million increase in trade and other payables arising from a $37 million foreign exchange increase and a $28 million timing difference on the payment of expenses associated with a patent litigation gain, which was partially offset by a $59 million decrease in bank overdrafts and loans and $18 million decrease in provisions.

CASH FLOW

Cash generated from operations of $1,273 million (2016: $1,035 million) is after paying out $3 million (2016: $24 million) of acquisition-related costs, $15 million (2016: $62 million) of restructuring and rationalisation expenses and $25 million (2016: $36 million) relating to legal and other costs.

Trading cash flow1 increased by $175 million primarily related to working capital movements.

Free cash flow1 increased by $257 million primarily related to working capital movements and lower cash outflows for acquisition-related costs, restructuring and rationalisation expenses and legal and other costs.

During the year ended 31 December 2017, the Group purchased a total of 3.2 million (2016: 24.0 million) ordinary shares at a cost of $52 million (2016: $368 million) as part of the ongoing programme to buy back an equivalent number of shares to those vesting as part of the employee share plans. 2016 share repurchases included a $300 million share buy-back programme following the disposal of the Gynaecology business.

DIVIDENDS

The 2016 final dividend of 18.5 US cents per ordinary share totalling $162 million was paid on 10 May 2017. The 2017 interim dividend of 12.3 US cents per ordinary share totalling $107 million was paid on 1 November 2017.

LIQUIDITY AND CAPITAL RESOURCES

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

The Group’s net debt decreased from $1,550 million at the beginning of 2017 to $1,281 million at the end of 2017, representing an overall decrease of $269 million.

At 31 December 2017, the Group held $155 million (2016: $38 million) in cash net of bank overdrafts. The Group had committed facilities available of $2,425 million at 31 December 2017 of which $1,425 million was drawn. Smith & Nephew intends to repay the $13 million of bank loans due within one year by using available cash and drawing down on the longer-term facilities.

The principal variations in the Group’s borrowing requirements result from the timing of dividend payments, acquisitions and disposals of businesses, timing of capital expenditure and working capital fluctuations. Smith & Nephew believes that its capital expenditure needs and its working capital funding for 2017, as well as its other known or expected commitments or liabilities, can be met from its existing resources and facilities.

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

RETURN ON INVESTED CAPITAL

Return On Invested Capital1 (ROIC) is a measure of the return generated on capital invested by the Group. It provides a metric for long-term value creation and encourages compounding reinvestment within the business and discipline around acquisitions with low returns and long payback. ROIC increased from 11.5% in 2016 to 14.3% in 2017 as a result of the improved operating profit, the lower tax rate and a stable asset base.

ROIC is defined as:

$$\frac{\text{Net Operating Profit less Adjusted Taxes}}{\text{(Opening Net Operating Assets +Closing Net Operating Assets)/2}}$$

14.3% +280bps
Return On
Invested
Capital1 (ROIC)
WHY THIS KPI IS IMPORTANT

ROIC measures the return generated on capital invested by the Group.

HOW WE PERFORMED

ROIC was up 280bps year-on-year driven by improved operating profit, the lower tax rate and a stable asset base.

1 These non-IFRS financial measures are explained and reconciled to the most directly comparable financial measure prepared in accordance with IFRS on pages 178–181.

RISK REPORT

OUR APPROACH TO RISK

OUR RISK MANAGEMENT PROCESS

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

In carrying out our business we face many risks and uncertainties and our Risk Management Policy and Enterprise Risk Management Manual ensure that our Risk Community can identify, review and report risks at every level of our business. At the very top of our structure is our Board, setting our risk appetite and monitoring the application of our risk framework through strategy, execution and practically through the outputs of regular risk ‘deep dives’ by the business and Group Risk Team. The Board cascades our risk appetite throughout our organisation through the Risk Committee, Risk Owner Community and our Management Group with a formal ‘bottom up’ process ensuring that risks are escalated back through the process to our Board and form our Principal Risks as appropriate. Providing rigour and independence across this process is our Executive Committee and the Group Risk Team. At the third line of defence is our Internal Audit Function, providing an annual opinion on the effectiveness of our Risk Management process to the Group Risk Committee chaired by the Chief Executive Officer and then to the Board and its committees.

Roles	Responsibilities
Board of Directors and Board Committees	– Responsible for regular oversight of risk management and for our annual strategic risk review – Monitors risks through Board processes (Strategy Review, Disclosures, M&A, Investments, Disposals) and Committees (Audit and Ethics & Compliance), management reports and deep dives of selected risk areas – Audit Committee is responsible for ensuring oversight of the process by which risks relating to the Company and its operations are managed and for viewing the operating effectiveness of the Group’s Risk Management process
	– Reviews external/internal environment for emerging risks

Group Risk Committee	– Reviews risk register updates from Business Areas – Identifies significant risks and assesses effectiveness of mitigating actions
Business area/ Product Risk Groups	– Business Area/Product Group Risk champion provides support to ensure a framework is designed and implemented for alignment to the requirements of the Enterprise Risk Management Framework – Carry out day-to-day risk management activities – Identify and assess risk – Implement strategy and mitigating actions to treat risk within Business/Product Risk Groups – Risk Champions lead regular risk register updates
Group Risk Team	– Manage implementation of all aspects of the Group's approach to Enterprise Risk Management including implementation of processes, tools and systems to identify, assess, measure, manage, monitor and report risks – Facilitates implementation and coordination through Risk Champions – Provides resources and training to support process – Prepares Board and Group Risk Committee reports based on Business Area and Product Group updates
Annual assessment of effectiveness – Internal audit and control functions	

RISK MANAGEMENT LIFE CYCLE – OUR SEVEN-STEP PROCESS

Our risk management life cycle was refreshed and updated in 2017 to align with our new approach to include Product Groups within our risk portfolio. Our Risk Management Policy was launched in May with sponsorship from the Chief Executive Officer and a revised manual aligning to the new structure was launched shortly after. Risks continue to be managed through a ‘bottom up’ and ‘top down’ process, with monthly oversight from the Executive Committee and quarterly reports to the Board Committees. An overview of our ‘seven step’ process can be found below:

An overview of the Risk Management and Reporting Process

7 Monitoring and review MONITORING of risks and actions by management, the accountable Executive and Board. Coordinated and ongoing monitoring of the internal and external risk environment to respond to emerging and horizon risks.	1 Risk Identification IDENTIFYING risks associated to achievement of our objectives by function and product and at the Group level. Early and continuous risk identification including existing and horizon risks.	2 Gross (inherent) Risk assessment ASSESSING the level of inherent (gross) risk.
6 Risk Reporting REPORTING the status of our most significant risks through the ‘bottom up’ business area processes and the ‘top down’ Executive		3 Current Control identification IDENTIFYING existing controls to mitigate risks

Committee and Board process. Demonstrating appropriate management of, and response to, our risk profile.

5	4
Risk Response Planning IDENTIFYING additional actions required to meet our expected risk tolerance level and ASSIGNING risk owners, timeframes and actions for ongoing management and reporting.	Net (residual) Risk ASSESSING the level of residual (net) risk after mitigation so that risk levels are managed within defined tolerance thresholds without being over controlled or foregoing desirable opportunities.

2017 PRINCIPAL RISKS

We assess our Principal Risks in terms of their potential impact on our ability to deliver our Strategic Priorities. These links are highlighted across the following pages and further information on the Strategic Priorities is found on page 10.

LEGAL AND COMPLIANCE RISKS

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

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

Risk Tolerance	Link to strategy	Oversight
In complying with legal and compliance requirements, we have an extremely low tolerance.	Compliance with applicable laws and regulations and doing the right thing is part of our licence to operate and underlies all our Strategic Priorities.	Ethics & Compliance Committee
Change from 2016		
No Change		

STRATEGIC PRIORITIES PAGE 10

Examples of risks

Actions taken by management

– Failure to act in an ethical manner consistent with our Code of Conduct.	– Ethics & Compliance Committee oversees our ethical and compliance practices.
– Violation of anti-corruption or healthcare laws, breach by employee or third party representative.	– All employees are required to undertake annual training and to certify compliance on an annual basis with our Code of Conduct and Business Principles.
– Failure to respond adequately to changes in legislation/regulation.	– Group monitoring and auditing programmes in place.
– Misuse or loss of personal information of patients, employees, research subjects, consumers or customers results in violations of data privacy laws, including General Data Protection Regulations.	– Confidential independent reporting channels for employees and third parties to report concerns.

CYBER SECURITY

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

Risk Tolerance	Link to strategy	Oversight
In managing our cyber risk and the possible disruption and reputational impact we have a low to moderate tolerance for Cyber Security Risk.	Given our strategic priority ‘Innovate for value’ and an increasing focus on connected products we must deliver our technology solutions in compliance with laws and regulations and in a way that protects any vulnerability to Cyber Risk.	Audit Committee

Change from 2016

Included as ‘other risk’ in 2016

STRATEGIC PRIORITIES PAGE 10

Examples of risks	Actions taken by management
– Loss of Intellectual Property/major data privacy breach or significant impact on business operations from Malware or Ransomware outbreak.	– Security information and event management (SIEM) in place providing real-time analysis of security alerts generated by applications and network hardware.
– Cyber Security is not considered in the design of new products with more products being connectable/having embedded software.	– Annual Penetration Testing, endpoint protection and Intrusion detection/prevention.
	– Annual Mandatory training and continuous awareness training for end-users.

– Security Governance structure in place including a Cyber Security Steering Committee.

NEW PRODUCT INNOVATION, DESIGN & DEVELOPMENT INCLUDING INTELLECTUAL PROPERTY

Our product portfolio is becoming increasingly complex, especially as we move to more innovative connected product technologies and our strategy of ‘owning the disease’. Our success relies on investing in safe products and platforms and aligned internal and external design and development innovation in order to compete effectively. The need to be nimble and considered in our approach to protecting our products, process and Intellectual Property is essential.

extremely low tolerance.

No Change

STRATEGIC PRIORITIES

PAGE 10

Risk Tolerance	Link to strategy	Oversight
In pursuit of our strategy to be innovative but safe in our product offering we have a moderate to high tolerance for risk.	Our Strategic Priority to ‘Innovate for Value’ depends heavily on our ability to continue to develop new innovative products and bring them to market.	Board

Change from 2016

No Change

STRATEGIC PRIORITIES PAGE 10

Examples of risks	Actions taken by management
– Insufficient long-term planning to respond to competitor disruptive entries into marketspace. – Inadequate innovation due to low R&D investment, R&D skills gap or poor product development	– Newly created Global Research & Development (R&D) organisation and governance framework providing strategic direction for allocation of R&D investments across all businesses.

execution.

– Lower value business segment investment, such as product maintenance and line extension projects.

– Competitors may assert patents or other intellectual property rights against the Company, or fail to respect the Company's intellectual property rights.

– R&D charter to transform our Innovation pipeline and drive our corporate strategy to Innovate for Value.

– Strengthened Clinical Affairs programme integrated with Global Marketing.

– Cross functional New Product Design and R&D processes focused on identifying new products and potentially disruptive technologies and solutions.

– Monitoring of external market trends and collation of customer insights to develop product strategies.

– Careful attention to intellectual property considerations.

QUALITY AND REGULATORY

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

Risk Tolerance	Link to strategy	Oversight
Our response to this risk continues to be critical and our ability to align and exceed the standards required to ensure safe and compliant products is the key driver for our extremely low tolerance for risk in this area.	Our Strategic Priority to 'Simplify and Improve our Business Model' requires us to operate effectively and efficiently and to produce compliant products of the highest quality to our customers.	Board Ethics & Compliance Committee

Change from 2016

Modified Principal Risk in 2017 – formerly included as Operational Risk – Quality and Business Continuity

STRATEGIC PRIORITIES PAGE 10

Examples of risks

– Defects in design or manufacturing of products supplied to, and sold by, the Company could lead to product recalls or product removal or result in loss of life or major injury.

– Significant non-compliance with policy, regulations or standards governing products and

Actions taken by management

– Comprehensive product quality processes and controls from design to customer supply are in place.

– Careful attention to intellectual property considerations.

– Standardised monitoring and compliance with quality management practices through our Global Quality Assurance

operations regarding registration, manufacturing, distribution, sales or marketing.

– Failure to obtain proper approvals for new or changed technologies, products or processes.

and Regulatory Affairs organisation.

– Incident management teams in place to respond immediately in the event of an incident relating to patient safety.

– Governance framework in place for reporting, investigating and responding to instances of product safety and complaints.

PRICING AND REIMBURSEMENT

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

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

Risk Tolerance	Link to strategy	Oversight
In implementing innovative pricing strategies, we have a moderate to high tolerance for risk and are willing to accept certain risks in pursuit of new business opportunities.	Our Strategic Priorities to 'Build a Strong Position in Established Markets' and to 'Focus on Emerging Markets' depends on our ability to sell our products profitably in spite of increased pricing pressures from governments.	Board

Change from 2016

No Change

STRATEGIC PRIORITIES PAGE 10

Examples of risks	Actions taken by management
– Reduced reimbursement levels and increasing pricing pressures.	– Development of innovative economic product and service solutions for both Established and Emerging Markets.
– Systemic challenge on number of elective procedures.	– Appropriate breadth of portfolio and geographic spread to mitigate exposure to localised risks.
– Lack of compelling health economics data to support reimbursement requests.	– Incorporating health economic components into the design and development of new products.

– Risk of adverse trading margins due to fluctuating foreign currency exchange rates across our main manufacturing countries (US, UK, Costa Rica and China) and where our products are sold.	– Emphasising value propositions tailored to specific stakeholders and geographies through strategic investment and marketing programmes. – Holding prices within acceptable ranges through global pricing corridors.

BUSINESS CONTINUITY AND BUSINESS CHANGE

Operating with a Global Remit, increased outsourcing and more sophisticated materials and product technology has made our manufacturing and supply chain process far more complex, leading to a greater potential for disruptive events. Ensuring our ability to continually execute and operate key sites and facilities in order to develop, manufacture and sell our products within this environment is a key strategic priority of the organisation. In addition, the pace and scope of our business 'change' initiatives increases the execution risk that benefits may not be fully realised, costs of these changes may increase, or that our business as usual activities may not perform in line with our plans.

Risk Tolerance	Link to strategy	Oversight
In operating our business, executing our change programmes and in managing our suppliers and facilities we have a low to medium tolerance for this risk.	Our Strategic Priority to 'Simplify and Improve our Business Model' requires us to operate effectively and efficiently and to ensure continuity of supply of products and services to customers.	Board

Change from 2016

STRATEGIC PRIORITIES PAGE 10

Modified Principal Risk in 2017 – formerly included as Operational Risk – Quality and Business Continuity

Examples of risks	Actions taken by management
– Failure or significant performance issues experienced at critical/single source facilities.	– Comprehensive product quality processes and controls are in place from design to customer supply.
– Disruption to manufacturing at single or sole source facility (lack of manufacturing redundancy).	– Emergency and incident management and business recovery plans are in place at major facilities and for key products and key suppliers.
– Supplier failure impacts ability to meet customer demand (single source suppliers).	– Second source suppliers identified for critical components or products.
– Natural disaster impacts ability to meet customer demand.	– Undertaking risk based review programmes for critical suppliers.
– Significant 'change' prevents our projects and programmes such as APEX achieving the intended benefits and disrupts existing business activities.	– Project Management Governance and toolkits and project Steering Committee Oversight to support successful execution of programme and projects. Executive Committee and Audit Committee oversight of Risks to change programmes.

– Political and economic ‘uncertainty’ in the countries in which we operate, e.g. Brexit.	– Brexit Steering Group regularly monitors the evolving impact of Brexit and oversees our response.

MERGERS AND ACQUISITIONS

As the Company grows to meet the needs of our customers and patients, we recognise that we are not able to develop all the products and services required using internal resources and therefore need to undertake mergers and acquisitions in order to expand our offering and to complement our existing business. In other areas, we may divest businesses which are no longer core to our activities. It is crucial for our long-term success that we make the right choices around acquisitions and divestments. We have a well-defined cross-functional process for managing risks associated with mergers and acquisitions that is subject to scrutiny from executive management and the Board of Directors.

Risk Tolerance	Link to strategy	Oversight
In acquiring new businesses and business models, we have a moderate to high tolerance for commercial risk and are willing to accept certain risks in pursuit of new business.	Our Strategic Priority to 'Supplement Organic Growth with Acquisitions' depends on our ability to identify the right acquisitions, to conduct thorough due diligence and to integrate acquisitions effectively.	Board

Change from 2016

No Change

STRATEGIC PRIORITIES PAGE 10

Examples of risks	Actions taken by management
– Failure to identify appropriate acquisitions or to conduct effective acquisition due diligence.	– Acquisition activity is aligned with corporate strategy and prioritised towards products, franchises and markets identified to have the greatest long-term potential.
– Failure to integrate newly acquired businesses effectively, including Company standards, policies and financial controls.	– Clearly defined investment appraisal process based on return on capital, in accordance with Capital Allocation Framework and comprehensive post-acquisition review programme.
	– Undertaking detailed and comprehensive cross-functional due diligence prior to acquisitions.
	– Compliance risks included as part of due diligence reviews, integration plans and reporting for acquisitions.

TALENT MANAGEMENT

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

Risk Tolerance	Link to strategy	Oversight
We have a moderate tolerance for this risk. Change from 2016 Included as 'other risk' in 2016	All our strategic priorities rely on ensuring we have the right talent within our organisation to deliver maximum efficiency in everything we do and to build strong leaders for the future.	Board

STRATEGIC PRIORITIES PAGE 10

Examples of risks	Actions taken by management
– Loss of key talent and lack of appropriate succession planning in context of required skill sets for future business needs. – Loss of competitive advantage due to an inability to attract and retain Top Talent. – Loss of intellectual capital due to poor retention of talent.	– Formal Talent Review process where the Executive Team has accountability for managing talent. – Identification of high performing individuals and practices to plan for the succession of key roles. – Consistent and robust performance Management process. – Development of strategic skills resourcing plan by functional areas.

Commercial execution

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

Risk Tolerance	Link to strategy	Oversight
In continuing to execute our priorities in an innovative, safe, profitable and compliant way we have a low to moderate tolerance level.	All Strategic Priorities	Board

Change from 2016

Modified Principal Risk in 2017 – previously incorporated into other principal risks

STRATEGIC PRIORITIES PAGE 10

Examples of risks

– Failure to adequately execute our strategy from high-level ambition to specific actions to make the ambition a reality.

– Inability to keep pace with significant product innovation and technical advances to develop commercially viable products.

– Failure to appropriately adapt our priorities and execution when conditions change meaning that transformational programmes do not deliver the expected outcomes.

– Failure to engage effectively with our key stakeholders to meet their evolving needs leading to loss of customers.

Actions taken by management

– Strengthened our commercial platform by creating a global commercial organisation with a remit to drive commercial performance across the Group through sales force excellence and pricing discipline.

– Newly created Global Research & Development organisation and supporting

governance framework.

– Improved Market Development and Launch Execution – Commitment to ‘win’ profitably in our target markets.

– Strategic planning process clearly linked to business and Group Risk.

– Global transformational programmes in place providing agile opportunities for efficiencies, growth and a strengthened competitive position.

DEEP DIVES COMPLETED IN THE YEAR (Group Risk Team/Board and Audit Committee Reviews)

During the year, the risks identified through the ‘bottom up’ and ‘top down’ processes were mapped against each other with the most significant risks forming our Principal Risks. These risks and our tolerance levels were discussed with each member of Executive Committee separately and collectively in August and were presented to the Board during the Strategy Review in September 2017. A further ‘bottom up’ exercise was carried out in November to validate that the risk profile had not significantly changed since the initial exercise in June. No changes were required to our risk profile as a result of this exercise, which was also formally validated by each Accountable Executive.

Throughout 2017, a number of different risk topics were presented to the Board and its Committee and specific ‘Deep Dive’ reviews were also completed by the Group Risk Team as follows.

Board and Audit Committee Deep Dives

Legal, Compliance and Quality

During the year the Ethics & Compliance Committee meetings considers papers from the quality and regulatory, legal and compliance teams. In 2017, the meetings have covered topics including preparation for General Data Protection Regulation (GDPR) in EU, Medical Device Regulations (MDR), FDA & Notified Body Inspection Activities, the Global Quality and Compliance Audit programme, Transactions with Compliance Risks and the outcome of significant Investigations.

Strategic: Research and Development and M&A

The Board has considered a report from the R&D team covering topics/risks in relation to execution, driving high value Innovation Projects and investment in Clinical Evidence and associated strategies to manage these risks. Each Board meeting considers Corporate Development. For 2017, this has focused on the lead up to, and our acquisition of, Rotation Medical. Retrospective reviews have also happened during the year on previous acquisitions compared to the expectations in the deal models.

Manufacturing Operations

Throughout the year, the Board has received presentations from the global operations team with oversight of operational matters, particularly relating to the manufacturing footprint and the risks associated with the current footprint and the proposals to mitigate these risks.

Functional Oversight

The Board and Audit Committee receive regular updates throughout the year from functions such as IT, Tax, Treasury and Financial operations. The Audit Committee also receives an update three times during the year on progress of risk management across the organisation.

IT/Cyber

The Audit Committee received reports on IT and Cyber security, including an assessment of the existing risks and benchmarking against industry standards.

HR

Annual discussion at the Board in relation to talent succession, culture and values.

Group Risk Team Deep Dives

A series of planned ‘Deep Dives’ have been completed in the year across our Business and Product Group Risk Areas, including PICO, Total Knees and ALLEVYN product Groups, Compliance and Europe/Canada Business Areas. These reviews have been newly introduced in 2017 to supplement reports provided to the Board and primarily cover an ‘independent’ assessment of compliance to the expected Risk Management Framework and in particular the adequacy of stated mitigating activities. The results are reported through the Risk Champions and Accountable Executives to the Audit Committee and are tracked and monitored to resolution by the Group Risk Team.

2018 RISK MANAGEMENT PLAN

Our work will continue in 2018 to evolve and strengthen our approach to managing risks across the organisation, including our business areas and product groups. We will continue to ensure a truly collaborative approach to risk management with risk accountability sitting squarely with management and a proactive Group Risk Function influencing decision making through effective challenge and timely consultation. 2018 will see innovation further driven through a new Global Enterprise Risk Management tool, more regular and sophisticated risk reporting across the organisation and further embedding Risk Appetite into decision making.

2018 RISK MANAGEMENT TIMELINE

Q1 2018	Q2 2018	Q3 2018	Q4 2018	Q1 2019
Internal Audit				
				– Risk Management Effectiveness Review report to the next Audit Committee
		– 2019 Risk Based Internal Audit Plan Preparation		
Deep dive risk reviews Group Risk Team				
			– Prepare 2019 Enterprise Risk Management Strategy	
– Refresh Enterprise Risk management Policy and process	– Risk Champion/Owner training	– Facilitate ‘top down’ review process		
	– Report to Audit Committee	– One to Ones with Executive Committee and Board	– Prepare Review of Principal Risks	
– Monthly reports to Executive Committee	– Monthly reports to Executive Committee	– Monthly reports to Executive Committee		
			– Report to Audit Committee	
Business/Product Risk Areas				
– Quarterly Risk Review by Senior Leadership Team	– Quarterly Risk Review by Senior Leadership Team	– Quarterly Risk Review by Senior Leadership Team	– Quarterly Risk Review by Senior Leadership Team	
	– Risk Register refresh and submission to Group Risk Team			
			– Risk Register refresh and submission to Group Risk Team annual	

			certification
Executive Committee		– ‘Top Down’ Review of Principal/Significant Risks	– Approve Principal Risks
Board		– Review of significant risks	
Audit Committee – Review and approval of the Group’s 2017 Risk Management Process and Viability Statement	– Receive report from the Group Risk Team and review Enterprise Risk Management process	– Receive report from the Group Risk Team and review Enterprise Risk Management process	– Review and approve Principal Risks

OUR VIABILITY STATEMENT

HOW WE ASSESS OUR PROSPECTS

During the year, the Board has carried out a robust assessment of the Principal Risks affecting the Company, particularly those which could threaten the business model. These risks and the actions being taken to manage or mitigate them are explained in detail on pages 42–46 of this Annual Report.

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

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

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

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

– Throughout the year, a number of deep dives into different risks were conducted by the Board, the Audit Committee and the Ethics & Compliance Committee looking into the nature of the risks and how they were mitigated, as detailed on page 46 of this Annual Report.

– Throughout the year, a number of deep dives into specific risk areas were conducted by the Group Risk Team, the results of which were presented to and discussed by the Audit Committee.

ASSESSMENT PERIOD

The Board have determined that the three-year period to December 2020 is an appropriate period over which to provide its Viability Statement. This period is aligned to the Group’s Strategic Planning process and reflects the Board’s best estimate of the future viability of the business.

2017 SCENARIOS MODELLED

Scenario 1 – Pricing Link to Principal Risks

	Link to Strategy
– Pricing and reimbursement pressures or currency exchange volatility (Principal Risk) – leading to a major loss of revenues and profits. Action taken: We have modelled a 1% reduction in annual price growth/decline for each year from 2018.	– Pricing and Reimbursement
Scenario 2 Operational risk – Execution risk – our inability to launch new products losing significant market share to the competition. Action taken: We have modelled a 1% reduction in annual volume growth rates each year from 2018.	
– Product liability claims – giving rise to significant claims and legal fees. Action taken: We have modelled a one-off significant product liability claim in 2019.	– New Product Innovation, Design & Development (including Intellectual property)
– Temporary loss of key production capability – resulting in our inability to manufacture a key product for a period of time. Action taken: We have modelled the loss of a factory, resulting in the loss of production and sales of a key product for two years from 2019.	– Commercial Execution
Scenario 3 – Legal regulatory and compliance risks – Regulatory measures – impacting our ability to continue to sell key products. Action taken: We have modelled the complete loss of revenue from a key product for each year from 2018.	– Legal and Compliance
– Bribery and corruption claims – giving rise to significant fines. Action taken: We have assumed a one-off significant fine in 2019.	– Quality and Regulatory
Scenario 4 – Cyber security – Inability to issue invoices or collect money for a period of time.	
– Action taken: We have modelled one of our key regions being unable to invoice sales and collect cash for one month in 2019.	– Cyber Security
Other – Political and economic forces – for example political upheaval, which could cause us to withdraw from a major market for a period of time. Action taken: We have modelled the loss of revenue and profits from a medium sized business due to withdrawal from a market from 2019.	– Business Continuity and Business Change

SCENARIO TESTING

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

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

We are satisfied that we have robust mitigating actions in place as detailed on pages 42–46 of this Annual Report. We recognise, however, that the long-term viability of the Company could also be impacted by other, as yet unforeseen, risks or that the mitigating actions we have put in place could turn out to be less effective than intended.

VIABILITY STATEMENT

Having assessed the principal risks, the Board has determined that we have a reasonable expectation that the Company will be able to continue in operation and meet its liabilities as they fall due over a period of three years from 1 January 2018. In our long-term planning we consider horizons of both five and ten years. However, as most of our efforts are focused on the coming three years, we have chosen this period when considering our viability.

Our conclusion is based on our current Strategic Plan approved by the Board in January 2018, having regard to longer-term strategic intentions, yet to be formulated in detail. However, we operate in a changing marketplace, which might cause us to adapt our Strategic Plans. In responding to changing external conditions, we will continue to evaluate any additional risks involved which might impact the business model.

By order of the Board, on 22 February 2018

Susan Swabey

Company Secretary

OUR BOARD OF DIRECTORS

A DIVERSE BOARD

ROBERTO QUARTA (68)

Chairman

Joined the Board in December 2013 and appointed Chairman following election by shareholders at the 2014 Annual General Meeting. He was also appointed Chairman of the Nomination & Governance Committee and a Member of the Remuneration Committee on that day.

Career and experience

Roberto is a graduate and a former Trustee of the College of the Holy Cross, Worcester (MA), US. He started his career as a manager trainee at David Gessner Ltd, before moving on to Worcester Controls Corporation and then BTR plc, where he was a divisional Chief Executive. Between 1985 and 1989 he was Executive VP of Hitchiner Manufacturing Co., Inc. He returned to BTR plc in 1989 as Divisional Chief Executive, where he was appointed to the main board. From here he moved to BBA Aviation plc, as CEO and then as Chairman, until 2007. He has held several board positions, including NED of Powergen plc, Equant N.V., BAE Systems plc and Foster Wheeler AG. His previous Chairmanships include Italtel SpA, Rexel S.A., IMI plc and SPIE SA. He is currently

OLIVIER BOHUON (59)

Chief Executive Officer

Joined the Board and was appointed Chief Executive Officer in April 2011. Olivier has announced his intention to retire by the end of 2018.

Career and experience

Olivier holds a doctorate in Pharmacy from the University of Paris and an MBA from HEC, Paris. He started his career in Morocco with Roussel Uclaf S.A. and then, with the same company, held a number of positions in the Middle East with increasing levels of responsibility. He joined Abbott in Chicago as head of their anti-infective franchise with Abbott International before becoming Pharmaceutical General Manager in Spain. He subsequently joined GlaxoSmithKline plc, rising to Senior Vice President & Director for European Commercial Operations. He then re-joined Abbott as President for Europe, became President of Abbott International (all countries outside of the US), and then President of their Pharmaceutical Division. He joined Smith & Nephew from Pierre Fabre,

GRAHAM BAKER (49)

Chief Financial Officer

Joined the Board as Chief Financial Officer on 1 March 2017 and elected by shareholders on 6 April 2017.

Career and experience

Graham holds an MA degree in Economics from Cambridge University and qualified as a Chartered Accountant and Chartered Tax Adviser with Arthur Andersen. In 1995, he joined AstraZeneca PLC where he worked for 20 years, holding multiple senior roles, including Vice President Finance & Chief Financial Officer, North America (2008 2010), Vice President, Global Financial Services (2010 2013) and Vice President, Finance, International (2013 2015) with responsibility for all emerging markets. Most recently, Graham was Chief Financial Officer of generic pharmaceuticals company Alvogen.

Chairman of WPP plc. He is a partner at Clayton Dubilier & Rice and a former member of the Investment Committee of Fondo Strategico Italiano S.p.A.

Skills and competencies

Roberto's career in private equity brings valuable experience to Smith & Nephew, particularly when evaluating acquisitions and new business opportunities. He has an in-depth understanding of differing global governance requirements having served as a director and chairman of a number of UK and international companies. Since his appointment as Chairman in April 2014, he has conducted a comprehensive review into the composition of the Board and its Committees, and conducted the search for new Non-Executive Directors, resulting in the appointment of Vinita Bali in 2014, Erik Engstrom and Robin Freestone in 2015, Angie Risley and Marc Owen during 2017, and Roland Diggelmann so far in 2018.

Nationality

American/Italian

where he was Chief Executive.

Skills and competencies

Olivier has extensive international healthcare leadership experience within a number of significant pharmaceutical and healthcare companies. His global experience provides the skillset required to innovate a FTSE 100 company with a deep heritage and provide inspiring leadership. He is a NED of Virbac Group and Shire plc, where he is also a member of the Remuneration Committee and the Nomination & Governance Committee and will be appointed Senior Independent Director on 25 April 2018.

Nationality

French

Skills and competencies

Graham has deep sector knowledge and has had extensive exposure to established and emerging markets which is extremely relevant to his role at Smith & Nephew. He has a strong track record of delivering operational excellence and has relevant experience across major finance roles and geographic markets, leading large teams responsible for significant budgets.

Nationality

British

VINITA BALI (62)

Independent Non-Executive Director

Appointed Independent Non-Executive Director in December 2014 and Member of the Remuneration Committee and Ethics & Compliance Committee.

Career and experience

Vinita holds an MBA from the Jamnalal Bajaj Institute of Management Studies, University of Bombay and a BA in Economics from the University of Delhi. She commenced her career in India with a Tata Group Company, and then joined Cadbury India, subsequently working with Cadbury Schweppes plc in the UK, Nigeria and South Africa. She has held a number of senior global positions in marketing and general management at The Coca-Cola Company based in the US and South America, becoming President of the Andean Division in 1999 and VP, Corporate Strategy in 2001. In 2003, she joined Zyman Group, LLC, a US based consultancy, as Managing Principal. Vinita was MD and CEO of Britannia Industries Limited, a leading Indian publicly listed food company from 2005 to 2014. Currently, Vinita is NED of Syngene International Limited, Titan Company Ltd, Bunge Limited and CRISIL India (a Standard & Poor Company). She is also Chair of the board of Global Alliance for Improved Nutrition and a member of the Advisory Board of PwC India.

Skills and competencies

IAN BARLOW (66)

Independent Non-Executive Director

Appointed Independent Non-Executive Director in March 2010, Chairman (now Member) of the Audit Committee in May 2010, Member of the Ethics & Compliance Committee in October 2014 and Senior Independent Director and Member of the Nomination & Governance Committee on 6 April 2017.

Career and experience

Ian is a Chartered Accountant with considerable financial experience both internationally and in the UK. He was a Partner at KPMG, latterly Senior Partner, London, until 2008. At KPMG, he was Head of UK tax and legal operations. Previously he was Chairman of WSP Group plc, and is currently NED and Chairman of the Audit Committees of The Brunner Investment Trust PLC, Foxtons Group plc and Urban&Civic plc.

Skills and competencies

THE RT. HON BARONESS VIRGINIA BOTTOMLEY OF NETTLESTONE DL (69)

Independent Non-Executive Director

Appointed Independent Non-Executive Director in April 2012 and Member of the Remuneration Committee and Nomination & Governance Committee in April 2014.

Career and experience

Virginia gained her MSc in Social Administration from the London School of Economics following her first degree. She was appointed a Life Peer in 2005 following her career as a Member of Parliament between 1984 and 2005. She served successively as Secretary of State for Health and then Culture, Media and Sport. Virginia was formerly a Director of Bupa and AkzoNobel NV. She is currently a Director of International Resources Group Limited, member of the International Advisory Council of Chugai Pharmaceutical Co., Chancellor of University of Hull and Sheriff of Hull and Trustee of The Economist Newspaper. She is the Chair of Board & CEO Practice at Odgers Berndtson.

Skills and competencies

Vinita has an impressive track record of achievement with blue-chip global corporations in multiple geographies including India, Africa, South America, US and UK, all key markets for Smith & Nephew. Additionally, her strong appreciation of customer service and marketing brings deep insight as we continue to develop innovative ways to serve our markets and grow our business.

Nationality

Indian

Ian's longstanding financial and auditing career and extensive board experience add value to his role as a member of the Audit Committee. As a member of the Ethics & Compliance Committee, he has managed to co-ordinate an oversight role of both Committees. This has been invaluable when commencing his role as Senior Independent Director with effect from 6 April 2017. Ian's first board evaluation is discussed in the corporate governance statement.

Nationality

British

Virginia's extensive experience within Government, particularly as Secretary of State for Health, brings a unique insight into the healthcare system both in the UK and globally, whilst her experience on the board of Bupa brings an understanding of the private healthcare sector and an insight into the needs of our customers. Her experience running the board practice at a search firm gives her a valuable skillset as a member of the Nomination & Governance Committee and Remuneration Committee. Her long association with Hull, the home of many of our UK employees, also brings an added perspective.

Nationality

British

ERIK ENGSTROM (54)

Independent Non-Executive Director

Appointed Independent Non-Executive Director on 1 January 2015 and Member of the Audit Committee.

Career and experience

Erik is a graduate of the Stockholm School of Economics (BSc) and of the Royal Institute of Technology in Stockholm (MSc). In 1988, he graduated with an MBA from Harvard Business School as a Fulbright Scholar. Erik commenced his career at McKinsey & Company and then worked in publishing, latterly as President and COO of Random House Inc. and as President and CEO of Bantam Doubleday Dell, North America. In 2001, he moved on to be a partner at General Atlantic Partners, a private equity investment firm. Between 2004 and 2009, he was CEO of Elsevier, the division

ROBIN FREESTONE (59)

Independent Non-Executive Director

Appointed Independent Non-Executive Director and Member of the Audit Committee and the Remuneration Committee on 1 September 2015 and Chairman of the Audit Committee on 6 April 2017.

Career and experience

Robin graduated with a BA in Economics from The University of Manchester and later qualified and commenced his career as a Chartered Accountant at Deloitte. He has held a number of senior financial positions throughout his career, including at ICI plc, Henkel Ltd and at Amersham plc. Robin was the Deputy CFO and then later the CFO of Pearson plc between 2006 and August 2015, where he was heavily involved with the transformation and diversification of Pearson. He was previously NED at eChem Ltd, Chairman of the 100 Group and Senior Independent Director and Chairman of the Audit Committee of Cable & Wireless Communications plc. Robin is a NED and Chairman of the Audit Committee at Moneysupermarket.com Group plc and Michael Kors Holdings Ltd. Robin became Chair of the ICAEW Corporate Governance Advisory Group in 2017.

MICHAEL FRIEDMAN (74)

Independent Non-Executive Director

Appointed Independent Non-Executive Director in April 2013 and Chairman of the Ethics & Compliance Committee in August 2014.

Career and experience

Michael graduated with a Bachelor of Arts degree, magna cum laude from Tulane University and a Doctorate in Medicine from the University of Texas Southwestern Medical Center. He completed postdoctoral training at Stanford University and the National Cancer Institute, and is board certified in Internal Medicine and Medical Oncology. In 1983, he joined the Division of Cancer Treatment at the National Cancer Institute and went on to become the Associate Director of the Cancer Therapy Evaluation Program. Michael was most recently CEO of City of Hope in California, and also served as Director of the institution’s cancer centre and held the Irell & Manella Cancer Center Director’s Distinguished Chair. He was formerly Senior VP of research, medical and public policy for Pharmacia Corporation and also Deputy Commissioner and Acting Commissioner at the US Food and Drug

specialising in scientific and medical information and then from 2009 CEO of RELX Group.

Skills and competencies

Erik has successfully reshaped RELX Group's business in terms of portfolio and geographies. He brings a deep understanding of how technology can be used to transform a business and insight into the development of new commercial models that deliver attractive economics. His experience as a CEO of a global company gives him valuable insights as a member of our Audit Committee.

Nationality

Swedish

JOSEPH PAPA (62)

Independent Non-Executive Director

Appointed Independent Non-Executive Director in August 2008 and Chairman of the Remuneration Committee in April 2011, Member of the Audit Committee and Ethics & Compliance Committee.

Joe will be retiring from the Board at the Annual General Meeting on 12 April 2018 and will not stand for re-election.

Nationality

American

Skills and competencies

Robin has been a well-regarded FTSE 100 CFO who has not only been heavily involved with transformation and diversification, but also the healthcare industry at Amersham, where his acquisition experience will be of value to Smith & Nephew as it continues to grow globally and in different markets. He brings financial expertise and insight as Chairman of the Audit Committee and an understanding of how to attract and retain talent in a global business as a member of the Remuneration Committee.

Nationality

British

Career and experience

Joe graduated with a Bachelor of Science degree in Pharmacy from the University of Connecticut and MBA from Northwestern University's Kellogg Graduate School of Management. In 2012, he received an Honorary Doctor of Science degree from the University of Connecticut School of Pharmacy. He began his career at Novartis International AG as an Assistant Product Manager and eventually rose to VP, Marketing, having held senior positions in both Switzerland and US. He moved on to hold senior positions at

Administration (FDA). He has served on a number of boards in a non-executive capacity, including Rite Aid Corporation. Currently, Michael is a NED of Celgene Corporation, MannKind Corporation and Intuitive Surgical, Inc.

Skills and competencies

Michael understands the fundamental importance of research, which is part of Smith & Nephew's value creation process. His varied experience in both the public and private healthcare sectors have given him a deep insight and a highly respected career. In particular his work with the FDA and knowledge relating to US compliance provides the skillset required to Chair the Ethics & Compliance Committee.

Nationality

American

Searle Pharmaceuticals and was later President & COO of DuPont Pharmaceuticals and later Watson Pharma, Inc. He was previously Chairman and CEO of Cardinal Health, Inc. and Chairman and CEO of Perrigo Company plc from 2006 to April 2016. Joe was appointed Chairman and CEO of Valeant Pharmaceuticals International, Inc. in May 2016.

MARC OWEN (58)

Independent Non-Executive Director

Appointed Independent Non-Executive Director and Member of the Audit Committee on 1 October 2017. To be appointed Member of the Ethics & Compliance Committee on 1 March 2018.

Career and experience

Marc graduated from Oxford University with a BA and BCL in Law. In 1984 he was called to the Bar, following four years at Corpus Christi College Cambridge as a fellow and director of studies in law. He decided upon a corporate career and undertook an MBA at Stanford University. Marc commenced his healthcare and technology career at McKinsey & Company where he progressed to senior partner and eventually a founding partner of McKinsey's Business Technology Office. In September 2001, Marc joined McKesson Corporation and served as Executive Vice President and member of the Executive Committee. He delivered strategic objectives and led over 40 acquisitions and divestments over a 10 year period. In late 2011 he headed Mckesson Speciality Health, which operates over 130 cancer centres across the US and provides services including market intelligence, supply chain services, patient access to therapy, provider and patient engagement and clinical trial support. His final executive

ANGIE RISLEY (59)

Independent Non-Executive Director

Appointed Independent Non-Executive Director and Chairman Elect of the Remuneration Committee on 18 September 2017.

Career and experience

After graduating from Exeter University, and completing a 1 year personnel management programme, Angie joined the United Biscuits graduate scheme. After working in various different HR roles she joined Pizza Hut (UK) Ltd as Human Resources Director, a joint venture between PepsiCo and Whitbread plc. After five years she joined Whitbread, becoming Executive Director on the plc board responsible for HR and Corporate Social Responsibility in 2004. Between 2007–2013 she was the Group HR Director for Lloyds Banking Group, joining J Sainsbury plc as Group HR Director in January 2013. Over the years, Angie has been a member of the Low Pay Commission and has held a number of non-executive directorships with Biffa plc, Arriva plc and Serco Group plc. She was a member of the Remuneration Committees at Arriva plc and Biffa plc and Chairman of the Remuneration Committee at Serco Group plc. She is also a NED on the Sainsbury's Bank Board.

ROLAND DIGGELMANN (51)

Independent Non-Executive Director

To be appointed Non-Executive Director and Member of the Audit Committee on 1 March 2018.

Careers and experience

Roland studied Business Administration at the University of Berne. In 1995, he joined Sulzer AG as Manager Strategic Planning and progressed into further senior roles over the years until his appointment as Executive Vice President, Sales Europe and Asia Pacific from 2002 to 2004 for Sulzer Medica (later known as Centerpulse). Roland joined Zimmer Group in 2004, in the role of Managing Director of Zimmer Japan and then later in 2006 as Senior Vice President, EMEA until 2008. Roland joined Roche Diagnostics in 2008 as president of Asia Pacific before his current appointment as the Chief Executive Officer of the Diagnostics Division of F. Hoffmann-La Roche Ltd.

Skills and experience

role came in 2014 where he was appointed Chairman of the European Management Board at Celesio AG. He retired in March 2017 once he had improved operations, set the strategy and recruited his successor.

Skills and competencies

Marc is a proven leader with an astute, strategic vision, capable of building significant international healthcare businesses. He has strong commercial healthcare expertise which the Board values deeply following the pending retirement of Joseph Papa at the 2018 Annual General Meeting.

Nationality

British

Skills and competencies

Angie is a well-regarded FTSE 100 Human Resources Director, proven NED and Remuneration Committee Chairman. She has gained experience in a wide range of sectors, including a regulated environment. This diversity of experience is welcomed by the Board and the Remuneration Committee. Angie is also additional resource and sounding board for our own internal Human Resources function.

Nationality

British

Having spent his whole career in medical devices, with 12 years at Sulzer and Zimmer, Roland brings an in-depth knowledge of the medical device industry and healthcare environment which will be of great value to Smith & Nephew, in particular following the retirement of Joseph Papa from the Board at the Annual General Meeting on 12 April 2018.

Nationality

Swiss

SUSAN SWABEY (56)

Company Secretary

Appointed Company Secretary in May 2009.

Nationality

British

Skills and experience

Susan has over 30 years' experience as a Company Secretary in a wide range of companies including Prudential plc, Amersham plc and RMC Group plc. Her work has covered board support, corporate governance, corporate transactions, group risk management, share registration, listing obligations, corporate social responsibility, pensions, insurance and employee and executive share plans. Susan is a member of the CBI Companies Committee and is a frequent speaker on corporate governance and related matters. She is also Chairman of the Board of Trustees of ShareGift, the share donation charity and a member of the Financial Reporting Council Lab Steering Group.

OUR LEADERSHIP

A STRONG TEAM

Olivier Bohuon is supported in the day-to-day management of the Group by a strong team of Executive Officers.

GRAHAM BAKER (49)

Chief Financial Officer

Joined the Board as Chief Financial Officer on 1 March 2017. Graham holds an MA degree in Economics from Cambridge University and qualified as a Chartered Accountant and Chartered Tax Adviser with Arthur Andersen. He is based in London, UK.

Skills and competencies

Graham has deep sector knowledge and has had extensive exposure to established and emerging markets which is extremely relevant to his role at Smith & Nephew. He has a strong track record of delivering operational excellence and has relevant experience across major finance roles and geographic markets, leading large teams responsible for significant budgets.

Nationality

British

GLENN WARNER (55)

President, US

Joined Smith & Nephew in June 2014 with responsibility for Advanced Wound Management's global franchise strategy, marketing and product development, as well as its US commercial business. With effect from 1 January 2016, Glenn became the President of Smith & Nephew's US business responsible for all the US commercial business. He is based in Fort Worth, US.

Skills and experience

Glenn has a broad-based background in pharmaceuticals and medical products including extensive international experience, having served most recently as AbbVie Vice President and Corporate Officer, Strategic Initiatives, where he was responsible for the development and execution of pipeline and asset management strategies. Prior to that he was President and Officer, Japan Commercial Operations in Abbott's international pharmaceutical business and Executive Vice President, TAP Pharmaceutical Products, Inc.

Nationality

American

RODRIGO BIANCHI (58)

President, International Markets

Joined Smith & Nephew in July 2013 with responsibility for Greater China, India, Russia, Asia, Middle East and Africa, focusing on continuing our strong momentum in these regions. With effect from 1 January 2016, Rodrigo also became responsible, for the Latin American, Australian, New Zealand and Japanese markets. His role was further expanded in May 2017, when he became responsible for oversight of the markets in Europe and Canada. He is based in Dubai, UAE.

Skills and experience

Rodrigo's experience in the healthcare industry includes 26 years with Johnson & Johnson in progressively senior roles. Most recently, he was Regional Vice President for the Medical Devices and Diagnostics division in the Mediterranean region and prior to that President of Mitek and Ethicon, Inc. He started his career at Procter & Gamble Italy.

Nationality

Italian

BRAD CANNON (50)

Chief Marketing Officer

Joined Smith & Nephew in 2012 and became President, Europe and Canada in March 2016. On 1 September 2017, he became Chief Marketing Officer. He is based in Andover, US.

Skills and experience

Brad was most recently President, Europe and Canada, where he successfully led the commercial business in those regions. Before that, he was President of Global Orthopaedic Franchises, leading Smith & Nephew's Reconstruction, Endoscopy, Trauma and Extremities businesses. Prior to Smith & Nephew, Brad worked in medtronic's Spine and Biologics division. From 2009, he was responsible for Medtronic's Spine International division and held positions heading US sales and global commercial operations. Brad is a graduate of Washington and Lee University, and the Wharton School of Business at the University of Pennsylvania.

Nationality

American

CATHY O'ROURKE (45)

Chief Legal Officer

Joined Smith & Nephew in February 2013 as Assistant General Counsel – Litigation & Investigations and became Chief Legal Officer in May 2017. Cathy heads up the Global Legal function and is based in Andover, US.

Skills and experience

Prior to joining Smith & Nephew, Cathy spent 11 years of her career with Davis Polk & Wardwell LLP. Cathy earned her Juris Doctorate in Law from Harvard University.

Nationality

American

MATTHEW STOBER (50)

President, Global Operations

Joined Smith & Nephew in October 2015 with responsibility for global manufacturing, supply chain, distribution, quality assurance, regulatory affairs, direct procurement, and manufacturing IT optimisation. He is based in Andover, US.

Skills and experience

Matt has more than 25 years' experience in healthcare manufacturing operations for global companies including Merck & Co., Inc. and GlaxoSmithKline plc. Most recently, he served as Senior Vice President, Corporate Officer and member of the Executive Committee at Hospira Pharmaceuticals. As a senior pharmaceutical operations executive with extensive technical and cross functional experience in start-up and complex challenging environments, Matt has led global and multi-company development projects, new product launches, critical quality-related turnarounds, network rationalisations and organisational transformations. He also has extensive experience working directly with external regulatory bodies, such as the US Food and Drug Administration.

Nationality

American

VASANT PADMANABHAN (51)

President of Research & Development

Joined Smith & Nephew in August 2016 and is responsible for Research and Innovation, New Product Development, Safety Affairs, Clinical Affairs, Medical Device/Pharmacovigilance and Clinical Operations. He is based in Andover, US.

Skills and experience

Vasant brings extensive experience in R&D and technology. Prior to Smith & Nephew, Vasant was Senior Vice President of Technical Operations at Thoratec Corporation, a leader in mechanical circulatory support solutions for the treatment of heart failure. In this role, he provided leadership to a 600 member team, with responsibility for global R&D, Program Management, Operations and Quality.Prior to Thoratec, Vasant had an 18 year career at Medtronic, starting as a Staff Scientist and, progressing through more senior roles, ultimately becoming Vice President of Product Development for the Implantable Defibrillator Business.Vasant holds a Ph.D degree in Biomedical Engineering from Rutgers University, USA and an MBA degree from the Carlson School of Management, Minnesota.

Nationality

American

CYRILLE PETIT (47)

Chief Corporate Development Officer and President, Global Business Services

Joined Smith & Nephew in May 2012 and leads the Corporate Development function and from October 2015 the Global Business Services. He is based in London, UK.

Skills and experience

Cyrille spent the previous 15 years of his career with General Electric Company, where he held progressively senior positions beginning with GE Capital, GE Healthcare and ultimately as the General Manager, Global Business Development of the Transportation Division. Cyrille began his career in investment banking at BNP Paribas and then Goldman Sachs.

Nationality

French

ELGA LOHLER (50)

Chief Human Resources Officer

Joined Smith & Nephew in January 2002 and became Chief Human Resources Officer in December 2015. Elga leads the Global Human Resources, Internal Communication and Sustainability Functions. She is based in London, UK.

Skills and experience

Prior to being appointed as Chief Human Resources Officer, Elga held progressively senior positions in Human Resources at Smith & Nephew in Wound Management, Operations, Corporate Functions and Group. Elga has more than 25 years' Human Resources experience.

Nationality

American/South African

OVERVIEW

COMMITTED TO THE HIGHEST STANDARDS OF CORPORATE GOVERNANCE

We maintain these standards through a clear definition of our roles, continuing development and evaluation and accountability through the work of the Board Committees.

LEADERSHIP
The Board sets the tone at the top of the Company through:

– A clear definition of the roles of the individual members of the Board.

– A comprehensive corporate governance framework.

– Defined processes to ensure the independence of Directors and the management of conflicts of interest.

Read more about our Board's Leadership on pages 57– 60

EFFECTIVENESS
The Board carries out its duties through:

– Regular meetings focusing on the oversight of strategy, risk (including viability) and succession planning.

– An annual review into the effectiveness of the Board.

– A comprehensive programme of development activities throughout the year.

Read more about our Board's Effectiveness on pages 61–65

ACCOUNTABILITY
The Board delegates some of its detailed work to the Board Committees:

REMUNERATION
The Remuneration Committee ensures that there is a formal and transparent

– Each Committee meets regularly and reports back to the Board on its activities. – The terms of reference of each Committee may be found on the Company's website at www.smith-nephew.com. – A report from the Chairman of each Committee is included in this Annual Report.	process for determining and reporting on the pay of our Executive Directors: – The Remuneration Policy was approved by shareholders at the 6 April 2017 Annual General Meeting. – The Committee ensures that: performance measures are linked to our strategic priorities; there is alignment between executive and shareholder interests; and our arrangements are simple to understand.
Read more about our Board's Accountability on pages 66–78	Read more about our Board's Remuneration on pages 79–105

The Board is committed to the highest standards of corporate governance and we comply with all the provisions of the UK Corporate Governance Code 2016 (the Code). The Company's American Depositary Shares are listed on the New York Stock Exchange (NYSE) and we are therefore subject to the rules of the NYSE as well as to the US securities laws and the rules of the Securities Exchange Commission (SEC) applicable to foreign private issuers. We comply with the requirements of the NYSE and SEC and have no significant differences to report between the UK and US corporate governance standards. We shall explain in this Corporate Governance Statement and in the reports on the Audit Committee, the Nomination & Governance Committee, the Ethics & Compliance Committee and the Remuneration Committee, how we have applied the provisions and principles of the Financial Conduct Authority's (FCA) Listing Rules, Disclosure & Transparency Rules (DTRs) and the Code throughout the year. The Code can be found at https://www.frc.org.uk/getattachment/ca7e94c4-b9a9-49e2-a824-ad76a322873c/UK-Corporate-Governance-Code-April-2016.

The Directors' Report comprises pages 6, 16-17, 25-28, 33-39, 42-78, 107, 140-142, 158 and pages 171-193 of the Annual Report.

COMPOSITION & ROLES

LEADERSHIP

COMPOSITION OF BOARD AS AT 31 DECEMBER 2017

We believe the Board's composition gives us the necessary balance of diversity, skills experience, independence and knowledge to ensure we continue to run the business effectively and deliver sustainable growth.

Diversity		Gender		Years of service		Ethnicity	
A EXECUTIVE	2	A MALE	9	A LESS THAN ONE YEAR	3	A WHITE	11
B NON-EXECUTIVE	9	B FEMALE	3	B ONE TO THREE YEARS	2	B ASIAN	1
C CHAIRMAN	1			C THREE TO SIX YEARS	4		
				D SIX TO NINE YEARS	2		
				E OVER NINE YEARS	1		

The Nomination & Governance Committee uses the following matrix when considering succession planning and future Board composition to ensure a balanced Board:

CEO 5 members of the Board are either current or recent CEOs	Financial 5 members of the Board have recent and relevant financial experience	International 7 members of the Board have international experience	Healthcare/ Medical Devices 5 members of the Board have different levels of experience within the Healthcare industry. The Board's medical devices experience will be strengthened with the appointment of Roland Diggelmann	Emerging market 2 members of the Board have Emerging Market experience
UK Governance 8 members of the Board have considerable	Remuneration 5 members of the Board have	Gender 9 members of the Board are male	Ethnic 11 members of the Board are white and 1 is Asian	Other Various Board members bring

experience of working in a UK listed environment and 6 members of the Board have experience of the US listed environment	Remuneration Committee experience within a UK listed context	and 3 are female	ethnicity	experiences in a variety of fields including customer focus, investment markets, government affairs, digital and corporate social responsibility

CHANGES TO THE BOARD

During the year to 31 December 2017 and since the year end, there were the following changes to the Board:

– Julie Brown retired from the Board as Chief Financial Officer on 11 January 2017.

– Graham Baker joined the Board as Chief Financial Officer on 1 March 2017.

– Brian Larcombe retired from the Board on 6 April 2017.

– Robin Freestone was appointed Chairman of the Audit Committee, succeeding Ian Barlow on 1 March 2017.

– Ian Barlow was appointed Senior Independent Director, succeeding Brian Larcombe on 6 April 2017.

– Angie Risley was appointed Non-Executive Director and Member and Chairman Elect of the Remuneration Committee on 18 September 2017.

– Marc Owen was appointed Non-Executive Director and Member of the Audit Committee on 1 October 2017. He will become a Member of the Ethics & Compliance Committee on 1 March 2018.

– Roland Diggelmann will join the Board as an additional Non-Executive Director and Member of the Audit Committee with effect from 1 March 2018.

RESPONSIBILITY & ACTIVITY

LEADERSHIP

ROLE OF DIRECTORS

Whilst we all share collective responsibility for the activities of the Board, some of our roles have been defined in greater detail. In particular, the roles of the Chairman and the Chief Executive Officer are clearly defined.

The roles of the Chairman, Non-Executive Directors, Senior Independent Director, Chief Executive Officer, Chief Financial Officer and the Company Secretary are defined as follows:

Chairman

– Building a well-balanced Board.

– Chairing Board meetings and setting Board agendas.

– Ensuring effectiveness of the Board and enabling the annual review of effectiveness.

– Encouraging constructive challenge and facilitating effective communication between Board members.

– Promoting effective Board relationships.

– Ensuring appropriate induction and development programmes.

– Ensuring effective two-way communication and debate with shareholders and stakeholders.

– Promoting high standards of corporate governance.

– Maintaining appropriate balance between stakeholders.

Chief Executive Officer

– Developing and implementing Group strategy.

– Recommending the annual budget and five-year strategic and financial plan.

– Ensuring coherent leadership of the Group.

– Managing the Group's risk profile and establishing effective internal controls.

– Regularly reviewing organisational structure, developing executive team and planning for succession.

– Ensuring the Chairman and Board are kept advised and updated regarding key matters.

– Maintaining relationships with shareholders and advising the Board accordingly.

– Setting the tone at the top with regard to compliance and sustainability matters.

– Day-to-day running of the business.

Chief Financial Officer

– Supporting the Chief Executive Officer in developing and implementing the Group strategy.

– Leading the global finance function, developing key finance talent and planning for succession.

– Ensuring effective financial reporting, processes and controls are in place.

– Recommending the annual budget and long-term strategic and financial plan.

– Maintaining relationships with shareholders.

Non-Executive Directors

– Providing effective challenge to management.

– Assisting in development and approval of strategy.

– Serving on the Board Committees.

– Providing advice to management.

Senior Independent Director

– Chairing meetings in the absence of the Chairman.

– Acting as a sounding board for the Chairman on Board-related matters.

– Acting as an intermediary for the other Directors where necessary.

– Available to shareholders and stakeholders on matters which cannot otherwise be resolved.

– Leading the annual evaluation into the Board's effectiveness.

– Leading the search for a new Chairman, if necessary.

Company Secretary

– Advising the Board on matters of corporate governance.

– Supporting the Chairman and Non-Executive Directors.

– Point of contact for investors on matters of corporate governance.

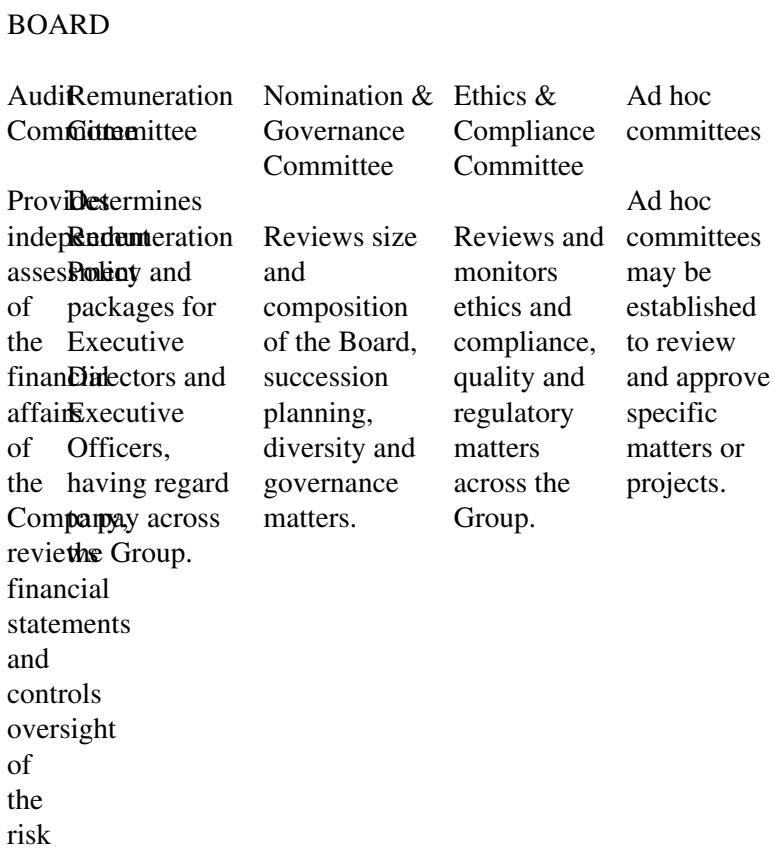
– Ensuring good governance practices at Board level and throughout the Group.

CORPORATE GOVERNANCE FRAMEWORK

The Board is responsible to shareholders for approving the strategy of the Group, for overseeing the performance of the Group and evaluating and monitoring the management of risk.

Each member of the Board has access, collectively and individually, to the Company Secretary and is also entitled to obtain independent professional advice at the Company's expense, should they decide it is necessary in order to fulfil their responsibilities as Directors.

The Board delegates certain matters, as follows, to Board Committees, consisting of members of the Board:



management process and key risks, such as cyber security. Manages use of internal and external auditors.				
Read more on page 71	Read more on page 79	Read more on page 66	Read more on page 69	

The Board delegates the day-to day running of the business to Olivier Bohuon, Chief Executive Officer, who is assisted in his role by the Executive Committee comprising the Executive Officers who are shown on pages 54–55 and certain other senior executives. The governance framework below outlines the Executive Committee arrangements as follows:

EXECUTIVE COMMITTEE
Recommends and implements strategy, approves budget and three-year plan, ensures liaison between commercial and corporate functions, receives regular reports from sub-committees, reviews major investments, divestments and capital expenditure proposals and approves business development projects.

Commercial Committee	Corporate Functions Committee	Portfolio Innovation Board	Regional leadership meetings	Functional leadership meetings
Recommends and implements strategy for global commercial functions and regions, managing sales, marketing,	Recommends and implements strategy for corporate functions identifying and executing new processes, systems and practices to improve operational	Defines portfolio allocation principles, reviewing and challenging current shape of portfolio, identifying gaps and opportunities and	Regional management through committees to drive regional performance.	Functional leadership teams to drive functional performance.

market access and commercial strategy and identifying and executing new processes, systems and practices to improve operational efficiency in commercial regions.	efficiency in corporate functions.	re-prioritising segments and geographies.		
Finance & Banking Committee Approves banking and treasury matters, guarantees, Group structure changes relating to mergers, acquisitions and disposals.	Disclosures Committee Approves release of communications to investors and Stock Exchanges.	Mergers & Acquisitions Council Oversees Corporate Development Strategy, monitors status of transactions and approves various stages in merger, acquisition and disposal process.	Group Risk Committee Reviews risk registers and risk management programme.	Group Ethics & Compliance Committee Reviews compliance matters and country business unit or function compliance reports.
Diversity & Inclusion Council Implements strategies to promote diversity.	Global Benefits Committee Oversees all policies and processes relating to pensions and employee benefit	Health, Safety & Environment Committee Oversees health, safety and environmental	IT Governance Board Oversees IT and cyber security.	

and plans. matters.
inclusion.

LEADERSHIP

INDEPENDENCE OF DIRECTORS

We require our Non-Executive Directors to remain independent from management so that they are able to exercise independent oversight and effectively challenge management. We therefore continually assess the independence of each of our Non-Executive Directors. The Executive Directors have determined that all our Non-Executive Directors are independent in accordance with both UK and US requirements. None of our Non-Executive Directors or their immediate families has ever had a material relationship with the Group. None of them receives additional remuneration apart from Directors' fees, nor do they participate in the Group's share plans or pension schemes. None of them serve as directors of any companies or affiliates in which any other Director is a director.

More importantly, each of our Non-Executive Directors are prepared to question and challenge management, to request more information and to ask the difficult questions. They insist on robust responses both within the Boardroom and, sometimes, between meetings. The Chief Executive Officer is open to challenge from the Non-Executive Directors and uses this positively to provide more detail and to reflect further on issues.

MANAGEMENT OF CONFLICTS OF INTEREST

None of our Directors or their connected persons, has any family relationship with any other Director or Officer, nor has a material interest in any contract to which the Company or any of its subsidiaries are, or were, a party during the year or up to 22 February 2018.

Each Director has a duty under the Companies Act 2006 to avoid a situation in which we have or may have a direct or indirect interest that conflicts or might conflict with the interests of the Company. This duty is in addition to the existing duty owed to the Company to disclose to the Board any interest in a transaction or arrangement under consideration by the Company.

If any Director becomes aware of any situation which might give rise to a conflict of interest, they must, and do, inform the rest of the Board immediately and the Board is then permitted under the Company's Articles of Association to authorise such conflict. This information is then recorded in the Company's Register of Conflicts, together with the date on which authorisation was given. In addition, each Director certifies on an annual basis that the information contained in the Register of Conflicts is correct.

When the Board decides whether or not to authorise a conflict, only the Directors who have no interest in the matter are permitted to participate in the discussion and a conflict is only authorised if the Board believes that it would not have an impact on the Board's ability to promote the success of the Company in the long term. Additionally, the Board may determine that certain limits or conditions must be imposed when giving authorisation. No actual conflicts have been identified, which have required approval by the Board. However, six situations have been identified which could potentially give rise to a conflict of interest and these have been duly authorised by the Board and are reviewed on an annual basis.

OUTSIDE DIRECTORSHIPS

We encourage our Executive Directors to serve as Non-Executive Directors of external companies. We believe that the work they do as Non-Executive Directors of other companies has benefits for their executive roles with the Company, giving them a fresh insight into the role of a Non-Executive Director. Olivier Bohuon is a Non-Executive Director of Shire plc and of Virbac Group. Olivier Bohuon discussed his external roles with the Chairman prior to accepting these appointments and the Chairman was satisfied that he had the capacity for the time commitment required.

RE-APPOINTMENT OF DIRECTORS

In accordance with the Code, all Directors offer themselves to shareholders for re-election annually, except those who are retiring immediately after the Annual General Meeting. Each Director may be removed at any time by the Board or the shareholders.

DIRECTOR INDEMNITY ARRANGEMENTS

Each Director is covered by appropriate directors' and officers' liability insurance and there are also Deeds of Indemnity in place between the Company and each Director. These Deeds of Indemnity mean that the Company indemnifies Directors in respect of any proceedings brought by third parties against them personally in their capacity as Directors of the Company. The Company would also fund ongoing costs in defending a legal action as they are incurred rather than after judgement has been given. In the event of an unsuccessful defence in an action against them, individual Directors would be liable to repay the Company for any damages and to repay defence costs to the extent funded by the Company.

LIAISON WITH SHAREHOLDERS

The Board meets with retail investors at the Annual General Meeting and responds to many letters and emails from shareholders throughout the year.

The Executive Directors also meet regularly with institutional investors to discuss the Company's business and financial performance both at the time of the announcement of results and at industry investor events. During 2017, the Executive Directors held meetings with institutional investors, including investors representing approximately 48% of the Company's share capital. Other topics discussed included strategy, market trends, reimbursement and regulatory changes, relevant macro-economic and political impacts on the business and the acquisition of Rotation Medical, Inc.

EFFECTIVENESS

During the early part of 2017, the Chairman, Roberto Quarta, held 17 meetings and telephone calls with investors holding approximately 22% of the Company's share capital. They discussed a range of topics including the performance of the Company during 2016, our strategic priorities, the structure of the Board, succession planning at Board and Executive level, diversity, the capital allocation framework and recent acquisitions.

Towards the end of 2017, Joseph Papa, the Chairman of the Remuneration Committee, took the opportunity of introducing Angie Risley, who will be succeeding him as Chairman of the Remuneration Committee on 12 April 2018, to eight of our key institutional shareholders holding around 15% of our share capital. They discussed the changes made to our remuneration policy, which were approved by shareholders at the 2017 Annual General Meeting and how the policy was being implemented. As well as giving shareholders the opportunity to meet Angie Risley, they also discussed the broad structure of remuneration arrangements proposed for the new Chief Executive Officer to be appointed following the retirement of Olivier Bohuon by the end of 2018. At the time of these meetings, there was no specific candidate identified as successor to Olivier Bohuon. They also discussed current trends and developments in executive remuneration.

Members of the Board are always happy to engage with investors, if they have matters they wish to raise with the non-executive team. Please contact the Company Secretary to arrange a suitable time to meet.

A short report on our major shareholders and any significant changes in their holdings since the previous meeting is reviewed at each Board meeting. The Chairman and Non-Executive Directors report back to the Board following their meetings with investors. Olivier Bohuon routinely reports on any concerns or issues that shareholders have raised with him in their meetings. Copies of the analyst reports on the Company and its peers are also circulated to Directors.

PURCHASE OF ORDINARY SHARES

In order to avoid shareholder dilution, shares allotted to employees through employee share schemes are bought back on a quarterly basis and subsequently cancelled as stated in Note 19.2 of the accounts on page 157.

RESPONSIBILITY OF THE BOARD

The work of the Board falls into the following key areas:

Strategy

– Approving the Group strategy including major changes to corporate and management structure.

– Approving acquisitions, mergers, disposals, capital transactions in excess of $50 million.

– Setting priorities for capital investment across the Group.

– Approving annual budget, financial plan, five-year business plan.

– Approving major borrowings and finance and banking arrangements.

– Approving changes to the size and structure of the Board and the appointment and removal of Directors and the Company Secretary.

– Approving Group policies relating to sustainability, health and safety, Code of Conduct and Code of Share Dealing and other matters.

– Approving the appointment and removal of key professional advisers.

Performance

– Reviewing performance against strategy, budgets and financial and business plans.

– Overseeing Group operations and maintaining a sound system of internal control.

– Determining the dividend policy and dividend recommendations.

– Approving the appointment and removal of the external auditor on the recommendation of the Audit Committee.

– Approving significant changes to accounting policies or practices.

– Overseeing succession planning at Board and Executive Officer level.

– Approving the use of the Company’s shares in relation to employee and executive share incentive plans on the recommendation of the Remuneration Committee.

EFFECTIVENESS

Risk

– Overseeing the Group’s risk management programme.

– Regularly reviewing the risk register.

– Overseeing risk management processes (see pages 40 and 41 for further details).

Shareholder communications

– Approving preliminary announcement of annual results, the publication of the Annual Report, the half-yearly report, the quarterly Trading Reports, the release of price sensitive announcements and any listing particulars, circulars or prospectuses.

– Approving the Sustainability Report.

– Maintaining relationships and continued engagement with shareholders.

Providing advice

– Using experience gained within other companies and organisations to advise management both within and between Board meetings.

The Schedule of Matters Reserved to the Board describes the role and responsibilities of the Board more fully and can be found on our website at www.smith-nephew.com.

BOARD TIMETABLE 2017

FEBRUARY

Early February

Approval of Preliminary Announcement

– Reviewed the results for the full year 2016 and the preliminary announcement and approved the final dividend to be recommended to shareholders for approval.

– Reviewed and approved the annual risk management report.

– Received updates on the progress of certain acquisitions over the past five years.

– Reviewed the results of the review into the effectiveness of the Board in 2016 and agreed action points for 2017.

– Reviewed and accepted that fees paid to Non-Executive Directors should remain unchanged.

Late February (via voice conference)

Approval of Financial Statements

– Reviewed and approved the Annual Report and Accounts for 2016, having determined that they were fair, balanced and understandable.

– Reviewed and approved the Notice of Annual General Meeting and related documentation.

– Approved the Budget for 2017 and the Strategic Plan for 2017 2021.

APRIL

– Received a review of recent acquisitions.

– Received an update on global operations.

– Reviewed the work of the Government Affairs function.

– Approved the Sustainability Report.

– Prepared for the Annual General Meeting to be held later that day.

MAY

(via voice conference)

– Reviewed the results for the first quarter 2017 and approved the Q1 Trading Report announcement.

JUNE

(via voice conference)

– Approved the appointment of Angie Risley as Non-Executive Director.

JULY

(in Hull, UK)

– Reviewed the results for the first half 2017 and approved the H1 announcement, having considered management's judgement in a number of areas, and approved payment of the interim dividend.

– Received and considered a report analysing the progress in Research and Development.

– Received and discussed the annual review of Group Insurances.

– Discussed the strategy review agenda for September 2017.

SEPTEMBER

(in Tokyo, Japan)

Strategy Review

– Conducted review of corporate strategy for 2018 2022.

– Reviewed the implications, risks and opportunities of the Medical Devices regulations.

– Approved the renewal of the directors' and officers' liability Insurance.

NOVEMBER

Early November (in Dubai, UAE)

Approval of Q3 Trading Report

– Reviewed the results for the third quarter 2017 and approved the Q3 Trading Report announcement.

– Received a follow up from Executive Officers from the Strategy Review in Tokyo in September.

– Received an update from Rodrigo Bianchi on the APAC/EM (Asia Pacific and Emerging Markets) business.

– Discussed the annual executive talent review.

Late November

Approval of Budget

– Reviewed the Budget for 2018.

– Received a review of the activities of Global Business Services.

– Received updates from Glenn Warner on the US Business.

In addition various matters were determined by written resolution, including accepting notice of the intention to retire of Olivier Bohuon as Chief Executive Officer and authorising the execution of certain agreements. Since the year end, we have also approved the Annual Report and Accounts for 2017 and have concluded that, taken as a whole, they are fair, balanced and understandable. We have approved the Notice of Annual General Meeting, recommended the final dividend to shareholders and have received and discussed the report on the effectiveness of the Board in 2017.

Each meeting was preceded by a meeting between the Chairman and the Non-Executive Directors without the Executive Directors and management in attendance. Unless otherwise stated, meetings are held in London, UK. At each meeting, we approved the minutes of the previous meetings, reviewed matters arising and received reports and updates from the Chief Executive Officer, the Chief Financial Officer, the Chief Corporate Development Officer, the Chief Legal Officer and the Company Secretary. We also received reports from the chairmen of the Board Committees on the activities of these Committees since the previous meeting.

BOARD AND COMMITTEE ATTENDANCE

Director	Board Member since	Board meetings (9 meetings)	Audit Committee meetings (7 meetings)	Remuneration Committee meetings (7 meetings)	Nomination & Governance Committee meetings (8 meetings)	Ethics & Compliance Committee meetings (4 meetings)
Roberto Quarta[1]	December 2013	9/9	–	6/7	8/8	–
Olivier Bohuon	April 2011	9/9	–	–	–	–
Graham Baker[2]	1 March 2017	7/7	–	–	–	–
Vinita Bali[3]	December 2014	7/9	–	6/7	–	4/4
Ian Barlow	March 2010	9/9	7/7	–	6/6	4/4
Virginia Bottomley	April 2012	9/9	–	7/7	8/8	–
Erik Engstrom	January 2015	9/9	6/7	–	–	–
Robin Freestone	September 2015	9/9	7/7	7/7	–	–
	April 2013	9/9	–	–	–	4/4

Michael Friedman						
Joseph Papa	August 2008	9/9	7/7	7/7	–	4/4
Marc Owen	1 October 2017	2/2	2/2	–	–	–
Angie Risley	18 September 2017	3/3	–	3/3	–	–
Brian Larcombe	March 2002	3/3	3/3	3/3	2/2	–

1 Roberto Quarta missed one Remuneration Committee meeting call convened on short notice. He had signified his approval of the matters being discussed to the Remuneration Committee Chairman prior to the meeting.

2 Graham Baker was appointed on 1 March 2017 and attended all his scheduled meetings to 31 December 2017.

3 Vinita Bali missed one Board call and one Remuneration Committee meeting on the same day, due to a prior commitment and one Board call convened on short notice. In each case, she had signified her approval of the matters being discussed to the Chairman prior to the meeting.

4 Erik Engstrom missed one Audit Committee meeting in Hull, which clashed with a RELX Board meeting, for which he is the Chief Executive Officer.

5 Marc Owen was appointed on 1 October 2017 and attended all his scheduled meetings to 31 December 2017.

6 Angie Risley was appointed on 18 September 2017 and attended all her scheduled meetings to 31 December 2017.

7 Brian Larcombe retired from the Board at the Annual General Meeting on 6 April 2017.

EFFECTIVENESS

BOARD EFFECTIVENESS REVIEW

The Board Effectiveness Review in 2017 was internally facilitated by Ian Barlow, Senior Independent Director assisted by the Company Secretary. The 2017 review comprised a questionnaire completed by each member of the Board. This questionnaire focused on the progress made addressing the issues raised in previous Board Evaluations as well as looking into how the Board had handled particular topics throughout the year. Ian Barlow then conducted individual interviews with each Board member. He also chaired a meeting of the Non-Executive Directors specifically to discuss the performance of the Chairman.

In January 2018, he prepared a report, detailing his findings, which he shared with the Chairman. The report was then discussed by the full Board in February 2018.

In discussion, we concluded that the Board worked well with a good breadth of skills, backgrounds and experience, which has been enhanced with the appointments during the past year. The culture was open and collaborative; the cadence of board meetings and the administrative support was broadly welcomed and we covered most of the right topics across the annual cycle. We did however identify some areas for further improvement as follows:

– Some changes could be made to the Board calendar to spread our work more efficiently and effectively throughout the year, with an even greater focus on people issues, R&D and commercial execution.

– We would like to spend more time on our site visits meeting the local teams, their staff, our customers and local hospitals to give us a deeper understanding of our markets, our customers and our competition and to assist in assessing bench strength further down the Company.

– Further improvements could be made to how we monitor performance against our strategic objectives, tracking development and implementation of strategy and lessons learned from our successes and shortfalls.

The areas for attention identified in the 2017 review had been addressed as follows:

Actions identified	Action taken
Gaining a deeper understanding of why our competitors are enjoying superior growth rates	During the year, as part of our site visits, the Board met with senior management in different territories and heard about the

compared with us so that we can help management identify, acquire and develop the resources they need to compete more effectively in our chosen markets.	commercial challenges faced in different markets. Part of the September Strategy Review included a focus on the different categories of customers and the pricing and reimbursement drivers which affect different business in different parts of the world.
Gaining a better understanding of the changing market dynamics in our chosen markets, focusing on identifying the different categories of customer and the pricing and reimbursement drivers which are in play, so that we can support and challenge management more effectively when they seek approval for projects to address these changing conditions.	We positively encourage our Non-Executive Directors to spend time with our sales representatives in order to experience the challenges they face first-hand.
Playing a more active role in supporting management develop robust succession plans for senior executive positions.	The Board reviews detailed succession plans on an annual basis. The Board also meets with potential successors to members of the management team during site visits and as part of Board presentations. During the year, Non-Executive Directors have assisted in the interview process for some senior management positions and have acted as a sounding board for the executive team, when considering succession plans in key areas.
Encouraging management to develop metrics and dashboards on a wider range of issues beyond financial metrics, particularly in the areas of Human Resources and R&D and ensuring that we regularly monitor progress against these metrics.	Dashboards have been developed throughout the year, which are reviewed at each Board meeting. These dashboards track progress against defined metrics with both a long-term and a short-term focus aligned to our Strategic Priorities, covering a wide range of business areas, including R&D, HR, the commercial and operating organisations, M&A and legal and compliance.

The last externally facilitated Board Effectiveness Review was carried out in 2015 by Belinda Hudson of Independent Audit.

The 2018 review will also be facilitated externally.

BOARD DEVELOPMENT PROGRAMME

Our Board Development Programme is directed to the specific needs and interests of our Directors. We focus the development sessions on facilitating a greater awareness and understanding of our business rather than formal training in what it is to be a Director. We value our visits to the different Smith & Nephew sites around the world, where we meet with the local managers of our businesses and see the daily operations in action. Meeting our local managers helps us to understand the challenges they face and their plans to meet those challenges. We also take these opportunities to look at our products and in particular the new products being developed by our R&D teams. This direct contact with the business in the locations in which we operate around the world helps us to make investment and strategic decisions. Meeting our local managers also helps us when making succession planning decisions below Board level.

All Non-Executive Directors are encouraged to visit our overseas businesses, if they happen to be travelling for other purposes. Our local management teams enjoy welcoming Non-Executive Directors to their business and it emphasises the interest the Board takes in all our operations. The Chairman regularly reviews the development needs of individual Directors and the Board as a whole.

The following development sessions covering both the Smith & Nephew business and wider market issues were held during the year:

July

– Visit to the Company’s site in Hull to take part in activities celebrating our 160th anniversary on the site. The Board toured the manufacturing and research facility and received presentations from members of the workforce involved in community focused activities as part of the Hull City of Culture 2017.

– Presentation from our Auditor, KPMG LLP (KPMG), on External Reporting trends, covering changing accounting standards and updates on financial reporting, the SEC and corporate governance changes relating to Audit Committees and Auditors.

September

– Presentations from the entire executive team as part of the Board’s Strategy Review, covering the whole business and including a discussion on Risk.

– Visit to the Company's offices in Tokyo and meetings with our senior leaders in Japan, with presentations on the business and challenges faced in Japan.

November

– Visit to the Company's offices in Dubai, the head office for our Emerging Markets businesses. The Board received presentations on our businesses in Saudi Arabia, India and Chile and met with the local General Managers in these countries.

– Presentation on the Emerging Markets business, including deep dives into Brazil, China and our Mid-Tier portfolio of products.

– Presentation on the US business discussing the opportunities and challenges faced by our different franchises across the US.

December

– Opportunities for our UK based Non-Executive Directors to go on the road with some of our London based sales representatives and for Vinita Bali to meet with representatives in Bangalore.

During the course of the year, we also received updates at the Board and Committee meetings on external corporate governance changes likely to impact the Company in the future.

INDUCTION PROGRAMME FOR NEW DIRECTORS

During 2017, Graham Baker, Angie Risley and Marc Owen joined the Board and each received tailored induction programmes relevant to their skills and experiences and their roles on the Board. These induction programmes, which are ongoing include:

– One-to-one meetings with senior executives to understand the roles played by our senior employees and specifically how we do things at Smith & Nephew;

– Visits to our sites local to the Director to get a feel of how our research and manufacturing operations are run;

– Opportunities to accompany our sales representatives on the road to better understand the daily challenges they face; and

– Meetings with our external advisers for example Freshfields, our Corporate lawyers, KPMG, our Auditor and Willis Towers Watson, our Remuneration Committee adviser to explain the legal and regulatory background to their role on our Board and how these issues are approached at Smith & Nephew.

By order of the Board, on 22 February 2018

Roberto Quarta

Chairman

NOMINATION & GOVERNANCE COMMITTEE REPORT

ACCOUNTABILITY

NOMINATION & GOVERNANCE COMMITTEE

Membership

	Member since	Meetings attended
Roberto Quarta (Chairman)	April 2014	8/8
Virginia Bottomley	April 2014	8/8
Ian Barlow1	April 2017	6/6
Brian Larcombe1	April 2011	2/2

1 Ian Barlow joined the Committee following the Annual General Meeting on 6 April 2017 on his appointment as Senior Independent Director. Ian replaced Brian Larcombe, who retired from the Board and the Nomination & Governance Committee following the Annual General Meeting on 6 April 2017.

2018 focus

– Appointment of new Chief Executive Officer to succeed Olivier Bohuon.

– Consider how best to ensure that the Board has considered different stakeholders in accordance with the proposals from the Government and the Financial Reporting Council.

DEAR SHAREHOLDER,

I am pleased to present the 2017 report of the Nomination & Governance Committee.

ROLE OF THE NOMINATION & GOVERNANCE COMMITTEE

Our work falls into the following two areas:

Board Composition

– Reviewing the size and composition of the Board.

– Overseeing Board succession plans.

– Recommending the appointment of Directors.

– Monitoring Board diversity.

Corporate Governance

– Overseeing governance aspects of the Board and its Committees.

– Overseeing the review into the effectiveness of the Board.

– Considering and updating the Schedule of Matters Reserved to the Board and the terms of reference of the Board Committees.

– Monitoring external corporate governance activities and keeping the Board updated.

– Overseeing the Board Development Programme and the induction process for new Directors.

– Identifying and monitoring any conflict of interests of the Board.

The terms of reference of the Nomination & Governance Committee describe our role and responsibilities more fully and can be found on our website: www.smith-nephew.com

ACTIVITIES OF THE NOMINATION & GOVERNANCE COMMITTEE IN 2017 AND SINCE THE YEAR END

In 2017, we held five physical meetings and three via teleconference. Each meeting was attended by all members of the Committee. The Company Secretary, Chief Executive Officer and Chief Human Resources Officer also attended all or some of the meetings by invitation and other Non-Executive Directors were invited to join the meetings to discuss the search for a new Chief Executive Officer. In between each meeting, various discussions were held between members of the Nomination & Governance Committee and the external search agent.

Our programme of work in 2017 was as follows:

Early February

Activities related to the year end

– Considered and approved the re-appointment of Directors who had completed three or six years' service and the annual appointment of Directors serving in excess of nine years.

– Recommended the appointment of Ian Barlow as Senior Independent Director to the Board following the retirement of Brian Larcombe and the appointment of Robin Freestone to replace Ian Barlow as Chairman of the Audit Committee.

– Reviewed and approved the Schedule of Matters Reserved to the Board and the terms of reference of the Board Committees.

– Discussed the search for two additional Non-Executive Directors.

April

Activities related to the appointment of Non-Executive Directors

– Considered candidates for the roles of Chairman Elect of the Remuneration Committee and a Non-Executive Director with Healthcare/Medical Devices experience.

August

Appointment of new Non-Executive Director

– Recommended to the Board that Marc Owen be appointed an additional Non-Executive Director.

Early September (by teleconference)

Update on search for additional Non-Executive Director

– Received an update on potential Non-Executive Director candidates with Medical Devices experience.

November (2 meetings)

Update on search for new Chief Executive Officer

– Received an update on the search for a new Chief Executive Officer.

December (2 meetings by teleconference)

Update on search for new Chief Executive Officer

– Discussed potential candidates for the role of Chief Executive Officer.

Further matters were resolved by written resolution including noting the retirement of Olivier Bohuon as Chief Executive Officer.

Since the year end, we have also discussed the future structure of the Board and completed our year end governance processes. We've also appointed Roland Diggelmann to the Board as an additional Non-Executive Director, who also

has strong Medical Devices experience.

The key areas of focus for us in 2017 were:

NON-EXECUTIVE DIRECTORS

Brian Larcombe retired as Senior Independent Director at the 2017 Annual General Meeting and Ian Barlow was appointed in his place. Ian Barlow has served on our Board as Chairman of the Audit Committee since 2010. He knows the Company well and has a sound understanding of the governance and regulatory requirements of the Board. He has also met some of our shareholders in his previous role as Chairman of the Audit Committee.

Robin Freestone took over the role of Chairman of the Audit Committee from Ian Barlow with effect from 1 March 2017. Robin had served as a Non-Executive Director of the Board and member of the Audit Committee and the Remuneration Committee for a period of 18 months. Prior to his appointment to the Board, he was a well-regarded FTSE 100 Chief Financial Officer who has brought relevant expertise and insight to the Audit Committee. His appointment as Chairman of the Audit Committee was designed to coincide with the appointment of Graham Baker to enable the Chief Financial Officer and Chairman of the Audit Committee to build a constructive working relationship together.

As we announced in the 2016 Annual Report, Joseph Papa will be retiring from the Board at the 2018 Annual General Meeting after more than nine years' service, seven of which as Chairman of the Remuneration Committee.

In the light of the departure of Brian Larcombe and Joseph Papa, the Nomination & Governance Committee analysed the skills and experiences required by the Board going forward to provide the necessary support and challenge to the executive team to execute against our Strategic Priorities. We used a matrix (see page 57) to compare these required skills and experiences against those already held by members of the Board and determined that we need to focus on:

– Increasing the diversity at Board level.

– Finding a replacement for Joseph Papa as Chairman of the Remuneration Committee.

– Replacing the investment knowledge and experience of Brian Larcombe.

– Reinforcing the Board with specific healthcare and Medical Devices experience.

During the year, we were advised by Zygos, who prepared a longlist of candidates for us and then worked with us to select a shortlist of candidates, who were interviewed by me and a number of other Non-Executive Directors. As a result of this process, we recommended to the Board that Angie Risley be appointed Non-Executive Director and Chairman Elect of the Remuneration Committee on 18 September 2017 and Marc Owen be appointed Non-Executive Director and member of the Audit Committee on 1 October 2017.

Angie Risley is a well-regarded FTSE 100 Human Resources Director and proven Non-Executive Director and Remuneration Committee Chairman with experience across a wide range of sectors, including a regulated environment. She will bring to the Board valuable experience of leading a Remuneration Committee as well as providing additional resource and sounding for our Human Resources function.

Marc Owen is a proven leader with an astute strategic vision, and experience of building significant international healthcare businesses. He has strong commercial healthcare expertise and general business experience, which will be of great value to the Company.

The appointment of Roland Diggelmann on 1 March 2018 will bring additional Medical Devices experience to our Board.

CHIEF EXECUTIVE OFFICER

In September 2017, Olivier Bohuon announced his intention to retire by the end of 2018. He chose to give us notice of this in order to give us time to find his successor. The Nomination & Governance Committee initiated a search in September 2017 advised by both Zygos and Russell Reynolds. Zygos does no other work for the Company other than advising on recruitment of Board members. Russell Reynolds also advises the Company on executive recruitment and appointments. This process is ongoing.

ACCOUNTABILITY

DIVERSITY

We aim to have a Board which represents a wide range of backgrounds, skills and experiences. We also value a diversity of outlook, approach and style in our Board members. We believe that a balanced Board is better equipped to consider matters from a broader perspective, understanding the views of our stakeholders as well as our shareholders and therefore come to decisions that have considered a wider range of issues and perspectives than would be the case in a more homogenous Board. Diversity is not simply a matter of gender, ethnicity or other easily measurable characteristics. Diversity of outlook and approach is harder to measure than gender or ethnicity but is equally important. A Board needs a range of skills from technical adherence to governance or regulatory matters to understand the business in which we operate. It needs some members with a long corporate memory and others who bring new insights from other fields.

There needs to be both support and challenge on the Board as well as a balance of gender and commercial and international experience. When selecting new members for the Board, we take these considerations into account, as well as professional background. A new Board member needs to fit in with their fellow Board members, but also needs to provide a new way of looking at things.

In 2012, we stated that our expectation would be that by 2015, 25% of our Board would be female and at the beginning and the end of 2017, we met this expectation, although the various Board changes during the year meant that this percentage fluctuated throughout the year. Looking forward, we shall work towards a Board with 33% female representation in-line with the Hampton-Alexander Review. We will also look to increase ethnic diversity on the Board following the Parker Review as appropriate. We will continue to appoint our Directors on merit, valuing the unique contribution that they will bring to the Board, regardless of gender, ethnicity or any other diversity measure.

In order to ensure that our Board remains diverse, we analyse the skills and experiences we require against the skills and experiences on our Board using the matrix on page 57. We review this matrix regularly to ensure that it is refreshed to meet the changing needs of the Company.

GOVERNANCE

During the year, the Nomination & Governance Committee also addressed a number of governance matters. We received updates from the Company Secretary on new developments in corporate governance and reporting in the UK

(and Europe). We reviewed the independence of our Non-Executive Directors, considered potential conflicts of interest and the diversity of the Board and made recommendations concerning these matters to the Board.

We have reviewed the proposals in the Government's Green Paper on corporate governance particularly in relation to enhancing the stakeholder voice. As a Board, we have identified our key stakeholders and during the course of 2018, we will be considering the best ways of ensuring that the voices of these different stakeholders are heard within the Boardroom.

SMITH & NEPHEW'S BROAD STAKEHOLDERS

EMPLOYEES	CUSTOMERS	GOVERNMENTS	INVESTORS
PAST	PATIENTS	REIMBURSEMENT	PAST
PRESENT	SUPPLIERS	INSURERS	PRESENT
FUTURE	SURGEONS/ NURSES	COMMUNITIES	FUTURE
	PROCUREMENT	PUBLIC	
		NGOS	

Roberto Quarta

Chairman of the Nomination & Governance Committee

ETHICS & COMPLIANCE COMMITTEE

Membership

	Member since	Meetings attended
Michael Friedman (Chairman)	August 2014	4/4
Vinita Bali	April 2015	4/4
Ian Barlow	October 2014	4/4
Joseph Papa1	April 2008	4/4

1 Joseph Papa will be retiring from the Board and the Committee at the Annual General Meeting to be held on 12 April 2018.

2 Marc Owen will join the Committee on 1 March 2018.

2018 focus

– Continue to monitor the impact of the EU General Data Protection Regulation (GDPR) and the EU Regulations for Medical Devices (MDR).

– Conduct select reviews of the compliance programme in key markets.

– Continue to monitor progress against key compliance and quality metrics.

DEAR SHAREHOLDER,

I am pleased to present the 2017 report of the Ethics & Compliance Committee.

ROLE OF THE ETHICS & COMPLIANCE COMMITTEE

Our work falls into the following two general areas:

Ethics & Compliance

– Overseeing ethics and compliance programmes, strategies and plans.

– Monitoring ethics and compliance process improvements and enhancements.

– Reviewing compliance performance based on monitoring, auditing and internal and external investigations data.

– Reviewing allegations of significant potential compliance issues.

– Receiving reports from the Group's Ethics & Compliance Committee meetings and from the Chief Compliance Officer and the Chief Legal Officer.

Quality Assurance and Regulatory Affairs (QARA)

– Overseeing the processes by which regulatory and quality risks relating to the Company and its operations are identified and managed.

– Receiving and considering regular functional reports and presentations from the President of Global Operations, SVP of Quality Assurance and other Officers.

The terms of reference of the Ethics & Compliance Committee describe our role and responsibilities more fully and can be found on our website: www.smith-nephew.com

ACTIVITIES OF THE ETHICS & COMPLIANCE COMMITTEE IN 2017 AND SINCE THE YEAR END

In 2017, we held four physical meetings. Each meeting was attended by all members of the Committee. The Company Secretary, the Chief Legal Officer, the Chief Compliance Officer, the SVP of Quality, and the President of Global Operations also attended all or part of the meetings by invitation.

Our programme of work in 2017 included the following:

February

– Reviewed various quality metrics including the level of complaints, the number and nature of field actions and the results of US Food and Drug Administration (FDA) inspections.

– Noted the progress made on the Global Compliance Programme Plan for 2016 and noted the plan of action for 2017.

April

– Reviewed various quality metrics and approved the Global Quality Plan for 2017, noting the additional work to be done in implementing the EU Medical Devices Regulation (MDR).

– Reviewed the actions taken to mitigate risk in new business ventures.

ETHICS & COMPLIANCE COMMITTEE REPORT

ACCOUNTABILITY

July (in Hull, UK)

– Reviewed various quality metrics including the results of inspections by the FDA and Notified Bodies, progress on handling complaints and in preparing for the MDR.

– Reviewed the progress being made to address findings identified by the Internal Audit function.

– Received an update regarding the Company’s readiness for the new EU General Data Protection Regulation (GDPR).

November (in Dubai, UAE)

– Reviewed various quality metrics including the results of inspections by the FDA and Notified Bodies, progress on handling complaints and preparations for the implementation of the MDR.

– Reviewed the progress against the 2017 Compliance Plan of Action and the follow up actions to findings identified in compliance audits.

At each meeting we noted and considered the activities of compliance and enforcement agencies and investigation of possible improprieties. At every meeting a report on the Quality Assurance Regulatory Assurance (QARA) function was provided along with updates of product complaint trends regularly discussed in 2017. We also reviewed a report on the activities of the Group’s Ethics & Compliance Committee and reviewed the progress of the Global Compliance Programme.

OVERSIGHT OF QUALITY & REGULATORY

Product safety is at the heart of our business. Regulatory authorities across the world enforce a complex series of laws and regulations that govern the design, development, approval, manufacture, labelling, marketing and sale of healthcare products. During the year, we oversaw the quality and regulatory activities of our business. At each meeting, we received a report on quality and regulatory matters from the SVP Quality and the President of Global Operations.

We reviewed the results of inspections carried out by the FDA and other regulators and monitored the progress of improvements following some of these inspections, using a dashboard, which highlighted progress being made. We also monitored the work being undertaken to help our manufacturing sites to prepare for future inspections.

We requested an in-depth report from management into our complaint handling process. This report explained our approach to complaint handling including, how we categorised different complaints, how we trained our staff to recognise and escalate complaints received by the business appropriately, and our planned and ongoing process enhancements.

We reviewed the results of quality audits undertaken during the year, approved follow up actions and monitored progress made to address these actions.

OVERSIGHT OF ETHICS & COMPLIANCE

'Doing the right thing' is part of our licence to operate. Business practices in the healthcare industry are subject to increasing scrutiny by government authorities in many countries. During the year, we oversaw the ethics and compliance activities of our business. At each meeting we received a report on ethics and compliance matters from the Chief Compliance Officer and a legal update on these matters from the Chief Legal Officer.

We regularly review our compliance programme as it relates to healthcare professionals and third party sellers (such as distributors and sales agents), particularly in higher risk markets. For healthcare professionals, this includes policies, training and certification, as well as pre-approval of consulting services and grants and fellowships. For third parties, our programme includes due diligence, contracts with compliance terms, compliance training and certification, and site assessments to check compliance controls and monitoring visits to review books and records.

We ensure that comprehensive due diligence is carried out prior to an acquisition and we ensure that following acquisitions new businesses are integrated rapidly into the Smith & Nephew compliance programme. During the year, we received a report from management on the ethics and compliance lessons learned from our mergers and acquisitions process over the last five years.

We oversee the employee compliance training programme, ensuring that all new employees are trained on our Code of Conduct, which sets out our basic legal and ethical principles for conducting business. We are updated on significant calls made to our whistle-blower line, which enables employees and members of the public to contact us anonymously through an independent provider (where allowed by local law) and are updated on allegations of potentially significant improprieties and the Company's response.

Michael Friedman

Chairman of the Ethics & Compliance Committee

AUDIT COMMITTEE
Membership

	Member since	Meetings attended
Robin Freestone (Chairman)1,2	September 2015	7/7
Ian Barlow1,2	May 2010	7/7
Erik Engstrom3	January 2015	6/7
Brian Larcombe4	January 2003	3/3
Marc Owen5	October 2017	2/2
Joseph Papa6	February 2011	7/7

1 Robin Freestone was appointed Chairman of the Audit Committee on 1 March 2017, succeeding Ian Barlow, who remained as a member of the Committee and became the Senior Independent Director with effect from 6 April 2017.

2 Designated financial experts under the SEC Regulations or recent and relevant financial experience under the UK Corporate Governance Code.

3 Erik Engstrom missed one Audit Committee meeting in Hull, which clashed with a RELX board meeting for which he is the Chief Executive Officer.

4 Brian Larcombe retired from the Board and Audit Committee at the Annual General Meeting on 6 April 2017.

5 Marc Owen was appointed to the Board and the Audit Committee with effect from 1 October 2017.

6 Joseph Papa will retire from the Board and the Audit Committee at the Annual General Meeting to be held on 12 April 2018.

7 Roland Diggelmann will join the Audit Committee on 1 March 2018.

2018 focus

– To provide assurance over the next phase of the Group’s NAPO system (our SAP Enterprise Resource Planning (ERP) implementation in North America).

– To extend the breadth of the assurance activities to include other risk areas such as product risk linking into the Group's top risk items.

– Monitoring the progress made on cyber security, one of our principal risks identified in 2017.

– To provide assurance over the Accelerating Performance and Execution (APEX) programme, which will streamline manufacturing, warehouse and distribution, use systems to provide general administration more efficiently and increase sales force effectiveness whilst maintaining customer focus.

DEAR SHAREHOLDER,

I'm pleased to write to you for the first time as your new Chairman of the Audit Committee. I must take this opportunity to thank Ian Barlow for his excellent chairmanship over the past seven years and wish him well in his new role as Senior Independent Director, whilst retaining his invaluable experience and expertise as he remains a member of the Audit Committee. I'd also like to thank Brian Larcombe, who stepped down on 6 April 2017, for his many years of wise counsel on this Committee.

Your Audit Committee has had another busy year, meeting seven times. Of course, the usual matters we expect to cover every year were dealt with, but as with all years there were other matters as well. Indeed there have been a number of personnel changes directly or indirectly affecting the Committee this year which I should reference:

We welcomed Graham Baker as our new Chief Financial Officer, with effect from 1 March 2017. Graham's profile can be read in the section about Directors on page 50 and he is an excellent appointment to the Board, including strong executive oversight of the Company's controls framework.

Marc Owen has also joined the Audit Committee. His background in healthcare, based in the US and European markets, provides the experience which will be missed by the anticipated retirement of Joe Papa in 2018. I'd like to welcome Marc to the Committee and look forward to working with him.

We welcomed Steve Humphries, our new SVP Internal Audit. Steve comes from a rich industry background. He was previously Chief Internal Auditor for SABMiller plc, another manufacturing firm, and brings strong insight. He has previously held positions at Wolseley plc, Avery Dennison Inc. and Néstle UK Ltd.

Finally, we welcomed our new Chief Information Officer, Chris Bayley, who has a strong background in cyber security from TUI plc. The work he has commenced has given the Committee the opportunity to review and challenge the IT architecture in the Company and its future-proofing to the ever present threat of cyber attack.

Moving onto our auditor, KPMG. They have completed their third year's audit and continue to provide robust challenge and suggest areas of improvement within our internal control framework. We have negotiated fees that will continue to be reviewed for good market practice. KPMG and the SVP Internal Audit's team continued to highlight areas where improvements are required. Further detail of the work undertaken can be found in the report below.

AUDIT COMMITTEE REPORT

ACCOUNTABILITY

The main non-routine matters we dealt with during the year were:

– Monitoring the improvements made in our risk management; led by Susan Swabey, Company Secretary, who is responsible for our risk management assessment. Susan has worked closely with our Senior Director of Internal Audit to develop our processes for risk management, our approach to risk appetite and improving alignment between the Board's assessment of risk and the underlying risk registers generated by management. This work accelerated in 2017 with deep dives to examine risk through the lens of our products and also considering risks from a cross-functional perspective.

– Monitoring the Company's Minimum Acceptable Practices (MAPs) for internal controls. We have set a goal of 97% compliance with these practices (currently 95% as self-assessed by management) and expect this to be achieved during 2018.

– Updates from our SVP Treasury, Tax and Finance Operations Functions. The SVP Tax reported on US tax reform.

– Monitoring the Finance Transformation project, which is planned to deliver significant cost savings and improvements to internal control and update on the service provided by our outsourced finance facility.

– Monitoring the progress of the implementation of our NAPO system (our SAP ERP implementation in North America).

– Assessing new accounting standards IFRS 9, 15 and 16.

– Update from Smith & Nephew's Chief Information Officer including cyber risk, IT risk as a whole and incident management reporting.

Robin Freestone

Chairman of the Audit Committee

ROLE OF THE AUDIT COMMITTEE

Our work falls into the following six areas:

Financial reporting

– Reviewing significant financial reporting judgements and accounting policies and compliance with accounting standards.

– Ensuring the integrity of the financial statements and their compliance with UK and US statutory requirements.

– Ensuring the Annual Report and Accounts are fair, balanced and understandable and recommending their adoption by the Board.

– Monitoring announcements relating to the Group's financial performance.

Internal controls

– Monitoring the effectiveness of internal controls and compliance with the UK Corporate Governance Code 2016 and the Sarbanes-Oxley Act, specifically sections 302 and 404.

– Reviewing the operation of the Group's risk mitigation processes and the control environment over financial risks.

Risk management

– On behalf of the Board, reviewing and ensuring oversight of the processes by which risks are managed, through regular functional reports and presentations, and reporting any issues arising out of such reviews to the Board.

– Reviewing the process undertaken and deep-dive work required to complete the Viability Statement and recommending its adoption to the Board.

– Reviewing the impact of risk management and internal controls and working closely with the Ethics & Compliance Committee.

Fraud and whistle-blowing

– Receiving reports on the processes in place to prevent fraud and to enable whistle-blowing.

– If significant, receive and review reports of potential fraud or whistle-blowing incidents.

Internal audit

– Agreeing Internal Audit plans and reviewing reports of Internal Audit work.

– Monitoring the effectiveness of the Internal Audit function.

– Reviewing the control observations made by the Internal Auditor, the adequacy of management's response to recommendations and the status of any unremediated actions.

External audit

– Overseeing the Board's relationship with the external auditor.

– Monitoring and reviewing the independence and performance of the external auditor and evaluating their effectiveness.

– Making recommendations to the Board for the appointment or re-appointment of the external auditor.

– Monitoring and approving the external auditor's fees.

The terms of reference of the Audit Committee describe our role and responsibilities more fully and can be found on our website, www.smith-nephew.com, where further information can be found for permitted non-audit services.

ACTIVITIES OF THE AUDIT COMMITTEE IN 2017 AND SINCE THE YEAR END

In 2017, we held five physical meetings and two meetings via voice conference. All except one meeting were attended by all appointed members of the Audit Committee. The Chairman, the Chief Executive Officer, the Chief Financial Officer, the SVP Internal Audit, the external auditor, and key members of the finance function, the Company Secretary and Deputy Company Secretary also attended by invitation. We also met with the external auditor and the SVP Internal Audit without management present. Our programme of work in 2017 was as follows:

Early February

Approval of Preliminary Announcement

– Reviewed the results for the full year 2016 and the preliminary announcement and recommended them for adoption by the Board.

– Reviewed a draft of the 2016 Annual Report.

– Reviewed the effectiveness of financial controls and of the Risk Management process and identified areas for improvement in 2017.

– Received a progress report from the SVP Internal Audit and approved the Internal Audit Plan for 2017.

– Received the Quality Assurance Report and approved the Quality Assurance work programme for 2017.

– Received the Viability Statement and confirmed that the Company is a viable entity for the assessed forthcoming three-year period.

– Confirmed the independence of KPMG as external auditor.

– Held a private meeting with external auditor, KPMG.

Late February (via voice conference)

Approval of Financial Statements

– Reviewed and approved the Annual Report and Accounts for 2016, having agreed that they were fair balanced and understandable, and recommended them for adoption by the Board.

– Considered the effectiveness and independence of the external auditor and concluded that their work had been effective and independent.

April

– Reviewed the control themes and observations of the external auditor and concluded that they had met expectations.

– Received a progress report from the SVP Internal Audit.

– Approved the Sustainability Report and its verification process.

– Received a corporate governance update for 2018 corporate reporting.

– Reviewed the annual report process and recommended improvements for 2017.

– Risk management update, including heat maps from the Company Secretary and Senior Director of Internal Audit.

– Held a private meeting with the external auditor, KPMG.

May (via voice conference)

Approval of Q1 Trading Report

– Reviewed the Q1 2017 Trading Report and approved the Q1 announcement.

– Approved the Company’s policy and report on Conflict Minerals for submission to the NYSE.

July (in Hull, UK)

Approval of H1 Results

– Reviewed the results for the first half 2017 and approved the H1 announcement.

– KPMG reviewed and provided findings on H1 2017.

– Reviewed and approved the external auditor’s Integrated Audit Plan for 2017.

– Received a progress report from the SVP Internal Audit.

– Received a report from the Group Treasurer, including an update on pension matters.

– Approved the definitions for trading/non-trading for annual reporting purposes.

– Received an update regarding the implementation of IFRS 9, 15 and 16.

– Held private meetings with external auditor, KPMG and the SVP Internal Audit.

Early November (in Dubai, UAE)

Approval of Q3 Trading Report

– Reviewed the Q3 2017 Trading Report and approved the Q3 announcement.

– Reviewed the progress reports from the external auditor on Q3 2017 and from Internal Audit on their work.

– Received an update on new reporting, regulatory and governance requirements.

– Received an update on Sarbanes-Oxley (SOx) and MAPs progress.

– Received a progress report from the SVP Internal Audit, focusing on fraud.

– Held a private meeting with the external auditor, KPMG.

Late November

Review of Functional Reports

– Received a report from the SVP Internal Audit focusing on the 2018 Internal Audit plan.

– Reviewed and approved the layout and design of the Annual Report 2017.

– Considered and approved critical accounting policies and judgements in advance of the 2017 year end.

– Received an update from KPMG on the external audit and preliminary SOx control findings.

– Received and discussed reports on Tax, Risk Management, Finance Transformation and Cyber Risk.

– Held private meetings with external auditor, KPMG and the SVP Internal Audit.

Since the year end, we have also reviewed the results for the full year 2017, the preliminary announcement, Annual Report and Accounts for 2017 and have concluded that taken as a whole, they are fair, balanced and understandable and have advised the full Board accordingly. In coming to this conclusion, we have considered the description of the Group’s strategy and key risks, the key elements of the business model, which is set out on pages 8–9, risks and the key performance indicators and their link to the strategy.

ACCOUNTABILITY

SIGNIFICANT MATTERS RELATED TO THE FINANCIAL STATEMENTS

We considered the following key areas of judgement in relation to the 2017 accounts and at each half-year and quarterly trading report, which we discussed in all cases with management and the external auditor:

Valuation of inventories

A feature of the Orthopaedic Reconstruction and Trauma & Extremities franchises (whose finished goods inventory makes up approximately 60% of the Group total finished goods inventory) is the high level of product inventory required, some of which is located at customer premises and is available for customers' immediate use. Complete sets of products, including large and small sizes, have to be made available in this way. These sizes are used less frequently than standard sizes and towards the end of the product life cycle are inevitably in excess of requirements. Adjustments to carrying value are therefore required to be made to orthopaedic inventory to anticipate this situation. These adjustments are calculated in accordance with a formula based on levels of inventory compared with historical usage. This formula is applied on an individual product line basis and is first applied when a product group has been on the market for two years. This method of calculation is considered appropriate based on experience, but it does involve management estimation of customer demand, effectiveness of inventory deployment, length of product lives, phase-out of old products and efficiency of manufacturing planning systems.

Our action

At each quarter end, we received reports from, and discussed with, management the level of provisioning and material areas at risk. The provisioning level was 19% at 31 December 2017 (20% as at 31 December 2016). We challenged the basis of the provisions and concluded that the proposed levels were appropriate and have been consistently estimated.

Liability provisioning

The recognition of provisions for legal disputes is subject to a significant degree of estimation. Provision is made for loss contingencies when it is considered probable that an adverse outcome will occur and the amount of the loss can

be reasonably estimated. In making its estimates, management takes into account the advice of internal and external legal counsel and uses third party actuarial modelling where appropriate. Provisions are reviewed regularly and amounts updated where necessary to reflect developments in the disputes. The ultimate liability may differ from the amount provided depending on the outcome of court proceedings and settlement negotiations or if investigations bring to light new facts.

Our action

As members of the Board, we receive regular updates from the Chief Legal Officer. These updates form the basis for the level of provisioning. The Group carries a provision relating to potential liabilities arising on its portfolio of modular metal-on-metal hip products of $157 million as of 31 December 2017. We received detailed reports from management on this position, including the actuarial model used to estimate the provision, and challenged the key assumptions, including the number of claimants and projected value of each settlement. The legal judgements have decreased by $35 million during the year, primarily due to settlements of a number of metal-on-metal matters that were provided for within the actuarially determined provision. There have been some smaller movements from cases having been resolved and some new matters arising. We have determined that the proposed levels of provisioning at year end of $190 million included within ‘provisions’ in Note 17.1 in 2017 ($225 million in 2016) were appropriate in the circumstances.

Impairment

In carrying out impairment reviews of acquisition intangible assets a number of significant assumptions have to be made when preparing cash flow projections. These include the future rate of market growth, discount rates, the market demand for the products acquired, the future profitability of acquired businesses or products, levels of reimbursement and success in obtaining regulatory approvals. If actual results should differ or changes in expectations arise, impairment charges may be required, which would adversely impact operating results.

Our action

We reviewed management’s reports on the key assumptions with respect to acquisition intangible assets – particularly the forecast future cash flows and discount rates used to make these calculations. We noted the reduction in headroom relating to the coblation technology asset acquired with ArthroCare in 2014 and challenged the assumptions used for future revenue growth of products using this technology. We concluded that the carrying value of this asset is appropriately supported by the cash flow projections. We have also considered the disclosure surrounding these reviews, and concluded that the review and disclosure were appropriate.

Taxation

The Group operates in numerous tax jurisdictions around the world. Although it is Group policy to submit its tax returns to the relevant tax authorities as promptly as possible, at any given time the Group has unagreed years outstanding and is involved in disputes and tax audits. Significant issues may take several years to resolve. In estimating the probability and amount of any tax charge, management takes into account the views of internal and external advisers and updates the amount of provision whenever necessary. The ultimate tax liability may differ from the amount provided depending on interpretations of tax law, settlement negotiations or changes in legislation.

Our action

We annually review our processes and approve the principles for management of tax risks. We review quarterly reports from management evaluating existing risks and tax provisions, which has included a detailed impact assessment of US tax reforms in the year end report from management. Based on a thorough report from management of tax liabilities and our challenge of the basis of any tax provisions recorded, we concluded that the levels of provisions and disclosures were appropriate.

OTHER MATTERS RELATED TO THE FINANCIAL STATEMENTS

As well as the identified significant matters, other matters that the Audit Committee considered during 2017 were:

Business combinations

During 2017, we acquired Rotation Medical, Inc. We received a report from management setting out the significant assets and liabilities acquired, details of the provisional fair value adjustments applied, an analysis of the intangible assets acquired, the assumptions behind the valuation of these acquired intangible assets and the proposed useful economic life of the intangible asset acquired. During 2017, we also considered and concurred with management that there had been no changes to the provisional fair values recognised in the 2016 acquisition of Blue Belt Technologies, Inc.

Post Retirement Benefit Pensions

The Group has post retirement defined benefit pension schemes, which require estimation in setting the assumptions. We received a report from management setting out their proposed assumptions for the UK and US schemes and concurred with management that these assumptions were appropriate.

EXTERNAL AUDITOR

Independence of External Auditor

Following a competitive tender in 2014, KPMG was appointed external auditor of the Company in 2015. We are satisfied that KPMG are fully independent from the Company's management and free from conflicts of interest. Our Auditor Independence Policy, which ensures that this independence is maintained, is available on the Company's website.

We believe that the implementation of this policy helps ensure that auditor objectivity and independence is safeguarded. The policy also governs our approach when we require our external auditor to carry out non-audit services, and all such services are strictly governed by this policy.

The Auditor Independence Policy also governs the policy regarding audit partner rotation with the expectation that the audit partner will rotate at least every five years. Stephen Oxley has been in tenure for three years as our Audit Partner. The Audit Committee confirms it has complied with the provision of the Competition and Markets Authority Order.

Effectiveness of external auditor(s)

We conducted a review into the effectiveness of the external audit as part of the 2017 year end process, in line with previous years. We sought the views of key members of the finance management team, considered the feedback from this process and shared it with management.

During the year, we also considered the inspection reports from the Audit Oversight Boards in the UK and US and determined that we were satisfied with the audit quality provided by KPMG.

The Audit Committee regularly receives feedback from KPMG, including at each meeting where management present their summary of critical accounting estimates as at each quarter end.

Overall therefore, we concluded that KPMG had carried out their audit for 2017 effectively.

The Audit Committee continues to review not only the effectiveness of the external auditor, KPMG but also its market competitiveness.

Appointment of External Auditor at Annual General Meeting

Resolutions will be put to the Annual General Meeting to be held on 12 April 2018 proposing the re-appointment of KPMG as the Company's auditor and authorising the Board to determine its remuneration, on the recommendation of the Audit Committee in accordance with the Competition and Markets Authority (CMA) Order 2014.

Disclosure of Information to the Auditor

In accordance with Section 418 of the Companies Act 2006, the Directors serving at the time of approving the Directors' Report confirm that, to the best of their knowledge and belief, there is no relevant audit information of which the Auditor, KPMG, is unaware and the Directors also confirm that they have taken reasonable steps to be aware of any relevant audit information and, accordingly, to establish that the Auditor is aware of such information.

ACCOUNTABILITY

Non-Audit Fees Paid to the Auditor

Non-audit fees are subject to approval in-line with the Auditor Independence Policy which is reviewed annually and forms part of the terms of reference of the Audit Committee.

The Audit Committee recognise the importance of the independence of the external auditor and ensures that the Auditor's independence should not be breached. The Audit Committee ensures that the Auditor does not receive a fee from the Company or its subsidiaries that would be deemed large enough to impact its independence or be deemed a contingent fee. The total fees for permitted non-audit services shall be no more than 70% of the average of the fees paid in the last three consecutive financial years for the statutory audits of the Company and its subsidiaries. In light of the Financial Reporting Council's revised Ethical Standards and SEC Regulations, we have revised our Auditor Independence Policy.

Any pre-approved aggregate, individual amounts up to $25,000 may be authorised by the Senior Vice-President Tax and Senior Vice-President Group Finance respectively and amounts up to $50,000 by the Chief Financial Officer. Any individual amount over $50,000 must be pre-approved by the Chairman of the Audit Committee. If unforeseen additional permitted services are required, or any which exceed the amounts approved, again pre-approval by the Chairman of the Audit Committee is required.

The following reflects the non-audit fees incurred with KPMG in 2017, which were approved by the Chairman of the Audit Committee:

		2017 $ million	2016 $ million
Tax fees and compliance services	Assistance with tax compliance in Singapore only.	0.1	0.1
Pension advice	Advice on the impact of changes to pension benefits for the UK defined benefit scheme.	–	0.5

Tax compliance services conducted by KPMG in 2017 only took place in countries where it is required by law for the auditor to conduct these services.

The ratio of non-audit fees to audit fees for the year ended 31 December 2016 was 0.15. The ratio of non-audit fees to audit fees for the year ended 31 December 2017 is 0.02.

Full details are shown in Note 3.2 of the Notes to the Group accounts.

Audit Fees paid to the Auditor

Fees for professional services provided by KPMG, the Group's independent auditor in each of the last two fiscal years, in each of the following categories were:

	2017 $ million	2016 $ million
Audit fees	4.4	4.0
Audit-related fees	–	–
Total	4.4	4.0

INTERNAL AUDIT

The Internal Audit team, which reports functionally to the Audit Committee, carries out risk-based reviews across the Group. These reviews examine the management of risks and controls over financial, operational, IT and transformation programme activities. The audit team, led by the SVP Internal Audit, consists of appropriately qualified and experienced employees. Third parties may be engaged to support audit work as appropriate.

The SVP Internal Audit has direct access to, and has regular meetings with, the Audit Committee Chair and prepares formal reports for Audit Committee meetings on the activities and key findings of the function, together with the status of management's implementation of recommendations. The Audit Committee has unrestricted access to all internal audit reports, should it wish to review them.

During the year, the team completed over 40 audits and reviews across the Group. These included reviews of: the roll-out of SAP across the North America business; IT operations including cyber status; inventory, financial reporting and credit management processes across multiple markets; Treasury operations; Manufacturing operations in China and Costa Rica; Shared Services operations in China, India and Poland; ERM effectiveness; and readiness for complying with e-commerce with key customers (GS1 GDSN) and Global Data Protection Requirements (GDPR).

A periodic review of the Internal Audit function is undertaken, most recently in 2014, by an independent external consultant in accordance with the guidelines of the Institute of Internal Auditors. In addition a structured questionnaire was introduced this year, allowing Non-Executive and Executive and senior management, plus the external auditor, to comment on key aspects of the function's performance. The Audit Committee, which re-approved the function's charter in November 2017, has satisfied itself that adequate, objective internal audit standards and procedures exist within the Group and that the Internal Audit function is effective.

RISK MANAGEMENT PROGRAMME

Whilst the Board is responsible for ensuring oversight of strategic risks relating to the Company, determining an appropriate level of risk appetite, and monitoring risks through a range of Board and Board Committee processes, the Audit Committee is responsible for ensuring oversight of the processes by which operational risks, relating to the Company and its operations are managed and for reviewing financial risks and the operating effectiveness of the Group's Risk Management process.

During the year, we reviewed our Risk Management processes and progress was discussed at our meetings in February, April and November. We approved the Risk Management Programme for 2017 and monitored performance against that plan specifically reviewing the work undertaken by the risk champions across the Group, identifying the risks which could impact their areas of our business.

During May and June, a new risk management policy and manual was rolled out with one-to-one training provided to risk champions. From May 2017, this allowed risk reporting to commence in-line with the strategy of a bottom up approach. This was revisited again in November. The Enterprise Risk Management (ERM) approach commenced and included interviewing individual members of senior management and the Board throughout Q3 2017, to discuss principal risks and concerns they had. These interviews were also used to understand the individual Board members' risk tolerance.

Later in July, the ERM structure was aligned with that of the Internal Audit function to assess the mitigating actions in place for our key products.

In November, it was reported that deep dives had concluded for ALLEVYN, Total Knees, Compliance EUCAN (Europe and Canada) and PICO, with key themes noted by the Committee. The 2017 Annual Report disclosure was also discussed.

Since the year end, we have reviewed a report from the SVP Internal Audit into the effectiveness of the Risk Management Programme throughout the year. We considered the principal risks, the actions taken by management to review those risks and the Board risk appetite in respect of each risk.

We concluded that the Risk Management process during 2017 and up to the date of approval of this Annual Report was effective. Work will continue in 2018 and beyond to continue to enhance the process.

See pages 40–49 for further information on our Risk Management Process.

VIABILITY STATEMENT

We also reviewed management’s work in conducting a robust assessment of those risks which would threaten our business model and the future performance or liquidity of the Company, including its resilience to the threats of viability posed by those risks in severe but plausible scenarios. This assessment included stress and sensitivity analyses of these risks to enable us to evaluate the impact of a severe but plausible combination of risks. We then considered whether additional financing would be required in such eventualities. Based on this analysis, we recommended to the Board that it could approve and make the Viability Statement on pages 48-49.

GOING CONCERN

The Group’s business activities, together with the factors likely to affect its future development, performance and position are set out in the ‘Financial review and principal risks’ section on pages 36–49. The financial position of the Group, its cash flows, liquidity position and borrowing facilities are described on pages 38-39.

In addition, the Notes to the Group accounts include the Group’s objectives, policies and processes for managing its capital; its financial risk management objectives; details of its financial instruments and hedging activities; and its exposure to credit risk and liquidity risk.

The Group has considerable financial resources and its customers and suppliers are diversified across different geographic areas. As a consequence, the Directors believe that the Group is well placed to manage its business risk successfully despite the ongoing uncertain economic outlook.

The Directors have a reasonable expectation that the Group has adequate resources to continue in operational existence for the foreseeable future. Thus they continue to adopt the going concern basis for accounting in preparing the annual financial statements.

Management also believes that the Group has sufficient working capital for its present requirements.

EVALUATION OF INTERNAL CONTROLS

Management is responsible for establishing and maintaining adequate internal control over financial reporting as defined in Rule 13a–15(f) and 15d–15(f) under the US Securities Exchange Act of 1934.

There is an established system of internal control throughout the Group and our country business units. The main elements of the internal control framework are:

– The management of each country is responsible for the establishment and review of effective financial controls within their business unit.

– The Group's IT organisation is responsible for the establishment of effective IT controls within the core financial systems and underlying IT infrastructure. The responsibility for the review of the effectiveness of such controls is split between the IT organisation and the Financial Controls & Compliance Group.

– The Group Finance Manual sets out financial and accounting policies. The Group's Minimum Acceptable Practices (MAPs) have been enhanced by simplifying and clarifying the requirements as well as broadening their scope. The business is required to self-assess their level of compliance with the MAPs twice a year and remediate any gaps. MAPs compliance is validated through spot checks conducted by the Financial Controls and Compliance function and during both Internal Audit and external audit visits.

– There are clearly defined lines of accountability and delegations of authority.

– During the year, there has been further progress in standardising and simplifying our core financial controls. In 2018, there will be a focus on standardising the controls globally, merging the core financial controls with the MAPs and evaluating technology solutions to operating and testing controls.

– The Internal Audit function executes a risk-based annual work plan, as approved by the Audit Committee.

– The Audit Committee reviews reports from Internal Audit on their findings on internal financial controls, including compliance with MAPs and from the SVP Group Finance and the heads of the Financial Controls and Compliance, Taxation and Treasury functions.

– The Audit Committee reviews regular reports from the Financial Controls and Compliance function with regard to compliance with the Sarbanes-Oxley Act including the scope and results of management's testing and progress regarding any remediation, as well as the aggregated results of MAPs self-assessments performed by the business.

– Business continuity planning, including preventative and contingency measures, back-up capabilities and the purchase of insurance.

– Risk management policies and procedures including segregation of duties, transaction authorisation, monitoring, financial and managerial review and comprehensive reporting and analysis against approved standards and budgets.

– A treasury operating framework and Group treasury team, accountable for all treasury activities, which establishes policies and manages liquidity and financial risks, including foreign exchange, interest rate and counterparty exposures. Treasury policies, risk limits and monitoring procedures are reviewed regularly by the Audit Committee on behalf of the Board.

– Our published Group tax strategy which details our approach to tax risk management and governance, tax compliance, tax planning, the level of tax risk we are prepared to accept and how we deal with tax authorities, which was reviewed by the Audit Committee on behalf of the Board.

ACCOUNTABILITY

– The Audit Committee reviews the Group whistle-blower procedures.

– The Audit Committee received and reviewed a report on the progress of the Finance Transformation during 2017 and the mitigation of the associated risks.

This system of internal control has been designed to manage rather than eliminate material risks to the achievement of our strategic and business objectives and can provide only reasonable, and not absolute, assurance against material misstatement or loss. Because of inherent limitation, our internal controls over financial reporting may not prevent or detect all misstatements. In addition, our projections of any evaluation of effectiveness in future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate. Entities where the Company does not hold a controlling interest have their own processes of internal controls similar to those of the Company.

We have reviewed the system of internal financial control and satisfied ourselves that we are meeting the required standards both for the year ended 31 December 2017 and up to the date of approval of this Annual Report. No concerns were raised with us in 2017 regarding possible improprieties in matters of financial reporting.

This process complies with the Financial Reporting Council's 'Guidance on Risk Management, Internal Control and Related Financial and Business Reporting' on the UK Corporate Governance Code and additionally contributes to our compliance with the obligations under the Sarbanes-Oxley Act and other internal assurance activities.

There has been no change during the period covered by this Annual Report that has materially affected, or is reasonably likely to materially affect, the Group's internal control over financial reporting.

The Board is responsible overall for reviewing and approving the adequacy and effectiveness of the risk management framework and the system of internal controls over financial, operational (including quality management and ethical compliance) processes operated by the Group. The Board has delegated responsibility for this review to the Audit Committee. The Audit Committee, through the Internal Audit function, reviews the adequacy and effectiveness of internal control procedures and identifies any weaknesses and ensures these are remediated within agreed timelines. The latest review covered the financial year to 31 December 2017 and included the period up to the approval of this Annual Report.

The main elements of this annual review are as follows:

- The Chief Executive Officer and the Chief Financial Officer evaluated the effectiveness of the design and operation of the Group's disclosure controls and procedures as at 31 December 2017. Based upon this evaluation, the Chief Executive Officer and Chief Financial Officer concluded on 22 February 2018 that the disclosure controls and procedures were effective as at 31 December 2017.
- Management is responsible for establishing and maintaining adequate internal control over financial reporting. Management assessed the effectiveness of the Group's internal control over financial reporting as at 31 December 2017 in accordance with the requirements in the US under section 404 of the Sarbanes-Oxley Act. In making that assessment, they used the criteria set forth by the Committee of Sponsoring Organisations of the Treadway Commission in Internal Control-Integrated Framework (2013). Based on their assessment, management concluded and reported that, as at 31 December 2017, the Group's internal control over financial reporting was effective based on those criteria.
- Having received the report from management, the Audit Committee reports to the Board on the effectiveness of controls.
- KPMG, an independent registered public accounting firm issued an audit report on the Group's internal control over financial reporting as at 31 December 2017.

CODE OF ETHICS FOR SENIOR FINANCIAL OFFICERS

We have adopted a Code of Ethics for Senior Financial Officers, which applies to the Chief Executive Officer, the Chief Financial Officer, the SVP Group Finance and the Group's senior financial officers. There have been no waivers to any of the Code's provisions nor have there been any amendments to the Code during 2017 or up until 22 February 2018. A copy of the Code of Ethics for Senior Financial Officers can be found on our website at www.smith-nephew.com

In addition, every individual in the finance function certifies to the Chief Financial Officer that they have complied with the Finance Code of Conduct.

EVALUATION OF COMPOSITION, PERFORMANCE AND EFFECTIVENESS OF THE AUDIT COMMITTEE

The composition, performance and effectiveness of the Audit Committee was evaluated this year in accordance with the EU Audit Reform. Its effectiveness is also reviewed in conjunction with the annual Board evaluation, which this year was conducted by Ian Barlow, in his first year as Senior Independent Director.

The review by the Audit Committee found the following and the below action will be taken during 2018:

Finding	Action
Composition	
The composition of the Audit Committee with at least one financial expert and a mix of UK and global experience in the healthcare sector was deemed appropriate.	None
Performance	
The Committee was considered to have performed effectively with an appropriate balance between challenge and constructive support.	None
Effectiveness	
The Committee was considered to be effective with a thorough agenda and papers, which were well presented and debated.	None

DIRECTORS' REMUNERATION REPORT

REMUNERATION

DEAR SHAREHOLDER,

This will be the final time I write to you as your Chairman of the Smith & Nephew plc Remuneration Committee. I have been a member of the Board since 2008 and Chairman of the Remuneration Committee since April 2011. With that longevity in mind, I will retire as Chairman of the Remuneration Committee and as a Director of the Company at the 2018 Annual General Meeting, where I will not stand for re-election. Much of my time during 2017 has been assisting our Chairman to find my replacement and assisting the new Remuneration Committee Chair in settling into her new role. I am very pleased to introduce Angie Risley to you as our Chairman Elect. Angie has vast experience of Human Resources, including remuneration and importantly was an effective member of the Remuneration Committee in her previous non-executive director roles, most recently as Chairman of the Remuneration Committee at Serco plc. Her experience in a wide variety of different sectors will add real value to what is becoming an expanded role for the Remuneration Committee. Proposed Corporate Governance changes indicate that increased employee engagement and oversight of employee remuneration generally will fall under the remit of the Remuneration Committee.

REVIEW OF 2017 PERFORMANCE

During the year, the Group delivered underlying revenue growth of 3% and a 20bps improvement in trading profit margin, in-line with guidance. Highlights included strong growth from Knee Implants and in the Emerging Markets. Trading cash flow improved year-on-year, at $940 million, as did the trading profit to cash conversion ratio of 90%. The tax rate on trading results reduced by 670bps to 17.1%, including a benefit from a one-off US tax settlement. Adjusted earnings per share (EPSA) were up 14%. Our Return On Invested Capital also improved, up 280bps to 14.3%.

These non-IFRS financial measures are explained and reconciled to the most directly comparable financial measure prepared in accordance with IFRS on pages 178–181.

As a result of the financial performance in 2017 and over the three-year period ending 31 December 2017, our Executive Directors received the following awards:

	Cash bonus (as % of salary)		Equity Incentive Award (as % of salary at date of grant)		Performance Share Award vesting (as % of salary at date of grant)	
Olivier Bohuon	91	%	50	%	102.6	%
Graham Baker	104	%	55	%	N/A	

The total remuneration paid to Olivier Bohuon and Graham Baker in 2017 is detailed further on page 83. As Graham Baker joined the Company on 1 March 2017, there are no comparative figures for him.

The single total remuneration figure for Mr Bohuon for 2017 increased to $5,032,925 from $3,332,850 in 2016. This was directly related to the stronger Company performance in 2017 and in particular above target performance for trading cash flow and trading profit margin, which collectively led to an increase of $616,009 for the Cash Incentive Plan. Our cumulative free cash flow and Emerging Market results over the three year performance period for our Performance Share Plan also contributed to a total vesting of these awards at 108% of target compared to 16% in 2016.

RETIREMENT OF OLIVIER BOHUON

You will see from the meetings the Remuneration Committee has conducted, 2017 was a busy year relating to Executive Director remuneration. Our Chairman, Roberto Quarta, has already touched on the retirement of Olivier Bohuon as Chief Executive Officer. The Committee has met to approve his retirement arrangements, which are in-line with the Remuneration Policy approved by our shareholders at the 2017 Annual General Meeting.

In summary, Olivier Bohuon will support the transition to the new Chief Executive Officer, when appointed and will continue to receive the same salary and benefits as in 2017. He will participate in the Annual Incentive Plan for the period worked in 2018, but will not receive a 2018 award under the Performance Share Plan. As a good leaver, his Equity Incentive Awards will vest on his leaving date, and his Performance Share Awards will be pro-rated for length of time served since the date of award and will vest subject to the original performance conditions on their original vesting dates in 2019 and 2020. Additionally, his 2017 award will remain subject to a two-year post vesting holding period.

I’d also like to personally thank Olivier for his leadership and improvements achieved during his tenure, and wish him the best for the future.

2017 ANNUAL GENERAL MEETING (AGM)

We were pleased that following the vote against our Remuneration Report (excluding the policy) in 2016, that both our Remuneration Policy and Remuneration Report received over 98% of votes in favour at the 2017 Smith & Nephew plc AGM. This demonstrates the strong support from our shareholders for our remuneration arrangements. We do not plan to make any changes to our remuneration arrangements in 2018.

I’d like to thank those shareholders who engaged with us during 2017 and met with Angie Risley. These shareholders covered nearly 15% of our shares. We welcome your feedback on our remuneration policy and arrangements and actively consider your views in our discussions.

LOOKING FORWARD

The Remuneration Committee will continue to be guided by the principles we have followed in the past:

– Performance measures linked to our strategic priorities;

– Alignment of executive and shareholder interests; and

– Simplicity.

We will ensure that pay remains aligned with performance.

We will also continue to monitor external corporate governance developments and respond accordingly, in particular those relating to expanding the remit of the Remuneration Committee to take greater account of the employee voice.

Joseph Papa

Chairman of the Remuneration Committee

REMUNERATION

MEASURES IN OUR VARIABLE PAY PLANS

Financial measures in Annual Incentive Plan	
Revenue (35%)	Revenue is a key driver of profit growth.
Trading Profit Margin (25%)	Trading profit margin is a critical measure both for the business and our shareholders and delivering margin improvements is a core commitment under our strategy.
Trading Cash Flow (15%)	Cash flow from our Established Markets is necessary in order to fund growth in Emerging Markets, innovation, organic growth and acquisitions.
Business objectives in Annual Incentive Plan	
Business Process (8.3%)	We need to release resources from the businesses through improved structures, efficiencies and business processes in order to re-invest in our higher growth areas, including Emerging Markets, innovation, organic growth and acquisitions.
People (8.3%)	We need to attract and retain the right people to achieve our strategy through improving our operating model and drive the right behaviours for all of our people globally.
Customer (8.3%)	Our mission is to deliver advanced medical technologies that help healthcare professionals, our customers and improve the quality of life of their patients.
Performance measures in our Performance Share Plan	
Relative TSR (25%)	If we execute our strategy successfully, this will lead to an increased return for our shareholders, whether you invest in the healthcare sector or in the FTSE.
Cumulative Cash Flow (25%)	Cash flow from our Established Markets is necessary in order to fund growth in Emerging Markets, innovation, organic growth and acquisitions.
Sales Growth (25%)	Sales growth is a key driver of profit growth.
Return on Invested Capital (25%)	Return on invested capital is a high priority for our shareholders which will drive better financial discipline and enhanced operating performance.

Detailed further on pages 97–101.

Compliance statement

We have prepared this Directors' Remuneration Report (the Report) in accordance with The Enterprise and Regulatory Reform Act 2012 2013 (clauses 81 84) and The Large and Medium-Sized Companies and Groups (Accounts and Reports) (Amendment) Regulations 2013 (the Regulations). The Report also meets the relevant requirements of the Financial Conduct Authority (FCA) Listing Rules.

The first part of the Report (pages 81–96) is the annual report on remuneration (the Implementation Report). The Implementation Report will be put to shareholders for approval as an advisory vote at the Annual General Meeting on 12 April 2018. The Implementation Report explains how the Remuneration Policy was implemented during 2017 and also how it is currently being implemented in 2018.

The second part of the Report (pages 97–105) is the Directors' Remuneration Policy Report (the Policy Report) which was approved by shareholders at the Annual General Meeting held in April 2017. The Policy Report describes our Remuneration Policy as it relates to the Directors of the Company. All payments we make to any Director of the Company will be in accordance with this Remuneration Policy. This Policy remains unchanged in 2018 and it is intended that it will next be put to shareholder vote at the Annual General Meeting to be held in 2020.

REMUNERATION COMMITTEE

Membership

	Member since	Meetings attended
Joseph Papa (Chairman)	April 2011	7/7
Angie Risley1 (Chairman Elect)	September 2017	3/3
Vinita Bali2	April 2015	6/7
Virginia Bottomley	April 2014	7/7
Robin Freestone	September 2015	7/7
Brian Larcombe3	September 2010	3/3
Roberto Quarta4	April 2014	6/7

1Angie Risley was appointed to the Board on 18 September 2017 and will be appointed Chairman of the Committee with effect from 12 April 2018, subject to her re-election.

2Vinita Bali was unable to attend one meeting due to a prior commitment. She had signified her approval of the matters being discussed to the Remuneration Committee Chairman prior to the meeting.

3Brian Larcombe retired from the Board at the Annual General Meeting on 6 April 2017.

4Roberto Quarta was unable to attend one meeting due to its short notice. He had signified his approval of the matter being discussed to the Remuneration Committee Chairman prior to the meeting.

2018 focus

– Evaluate remuneration package for a new Chief Executive Officer.

– Review gender pay reports and approve the implementation of a programme designed to reduce the gender pay gap.

– Consider possible response to BEIS Green Paper on Corporate Governance and how best to engage with our employees on remuneration matters.

– Consider the implications of US tax reform.

The Remuneration Committee presents the Annual Report on remuneration (the Implementation Report), which will be put to shareholders for an advisory vote at the Annual General Meeting to be held on 12 April 2018.

ROLE OF THE REMUNERATION COMMITTEE

Our work falls into the following three areas:

Determination of Remuneration Policy and Packages

– Determination of Remuneration Policy for Executive Directors and senior executives.

– Approval of individual remuneration packages for Executive Directors and Executive Officers, at least annually, and any major changes to individual packages throughout the year.

– Consideration of remuneration policies and practices across the Group.

– Approval of appropriate performance measures for short-term and long-term incentive plans for Executive Directors and senior executives.

– Determination of pay-outs under short-term and long-term incentive plans for Executive Directors and senior executives.

Oversight of all Company Share Plans

– Determination of the use of long-term incentive plans and overseeing the use of shares in executive and all-employee plans.

Reporting and Engagement with shareholders on Remuneration Matters

– Approval of the Directors' Remuneration Report ensuring compliance with related governance provisions.

– Continuation of constructive engagement on remuneration matters with shareholders.

The terms of reference of the Remuneration Committee describe our role and responsibilities more fully and can be found on our website: www.smith-nephew.com

ACTIVITIES OF THE REMUNERATION COMMITTEE IN 2017 AND SINCE THE YEAR END

In 2017, we held seven meetings and determined six matters by written resolution. Each meeting was attended by all members of the Committee (except Vinita Bali and Roberto Quarta who each missed one meeting this year). The Chief Executive Officer, the Chief Human Resources Officer and the SVP Global Reward, key members of the finance function and the Company Secretary also attended all or part of some of the meetings, except when their own remuneration was being discussed. We also met with the independent Remuneration Consultants, Willis Towers Watson, without management present. Our programme of work in 2017 can be found in the report below.

REMUNERATION
Early February

Approval of salaries, awards and payouts in 2017

– Agreed the targets for the short-term and long-term incentive plans for 2017. Introduced global revenue growth and ROIC as long-term performance measurements (defined on page 89). Approved the remuneration strategy for 2017 against the proposed business plan.

– Approved the quantum of cash payments to Executive Directors and Executive Officers under the Annual Incentive Plan and awards under the Equity Incentive Programme and the Performance Share Programme, having considered the 2016 financial results against the performance targets, that were set.

– The Audit Committee joined the Remuneration Committee for both of the above agenda items to answer any questions regarding audited numbers and provide assurance.

– Reviewed the salaries of the Board, Executive Directors and Officers and Chairman.

– Approved the text of the Remuneration Report.

Mid February

Review of Remuneration (via voice conference)

– Discussed the payout under the Annual Incentive Plan and decided to use downwards discretion to adjust outcomes following the performance of the Company in 2016.

Late February

Final approval of the Remuneration Report (via voice conference)

– Approved the final targets for the short-term and long-term incentive plans for 2017.

– Approved the final text of the Remuneration Report.

July (in Hull, UK)

Mid-year Review of Remuneration Arrangements

– Reviewed the shareholder response to the Remuneration Report at the Annual General Meeting and noted shareholders' feedback that would be addressed in this report.

– Reviewed the performance of long-term awards granted in 2015, 2016 and 2017.

– Discussed and planned a programme of engagement with institutional investors on remuneration.

– Considered termination arrangements for Executive Directors and Executive Officers.

– Reviewed adherence to shareholding guidelines by Executive Directors, Executive Officers and senior executives.

– Monitored dilution limits and the number of shares available for use in respect of executive and all-employee share plans.

– Approved amendments to the Smith & Nephew ShareSave Plan 2012 rules to reflect regulatory changes.

October

– Approved retirement package for Olivier Bohuon, Chief Executive Officer.

Early November (in Dubai, UAE)

– Prepared for meetings with shareholders to solicit viewpoints and introduce Angie Risley.

– Reviewed first draft of the Remuneration Report for 2017.

Late November

Review of Remuneration Strategy

– Received a report from the Chairman of the Remuneration Committee on recent engagement with shareholders.

– Reviewed and considered the principles for determining payouts under the long-term plans due to vest in 2018.

– Approved the final Remuneration Strategy for 2018.

– Reviewed market data for the Executive Directors and Executive Officers prepared in accordance with the agreed methodology.

Six written resolutions were approved during the year relating to the approval of remuneration arrangements for various Executive Officers.

Since year end, we have also reviewed the financial results for 2017 against the targets under the short-term and long-term incentive arrangements jointly with the Audit Committee, and have agreed the targets for the short-term and long-term incentive plans for 2018. We have also approved increases to the salaries of Executive Directors and Executive Officers and determined cash payments under the Annual Incentive Plan, awards under the Equity Incentive Programme and the Performance Share Programme, and the vesting of awards under the Performance Share Programme granted in 2015. Finally, we approved the wording of this Directors' Remuneration Report.

During the year, the Remuneration Committee received information and advice from Willis Towers Watson, an independent executive Remuneration consultancy firm appointed by the Remuneration Committee in 2011 following a full tender process. They provided advice on market trends and remuneration issues in general, attended Remuneration Committee meetings, assisted in the review of the Directors' Remuneration Report, provided market benchmark data on compensation design and levels, undertook calculations relating to the TSR performance conditions, assisted in matters relating to the Chief Executive Officer's retirement, and advised on investor views and engagement. In addition, the Committee received independent advice from Mercer relating to the use of discretion downwards when determining the level of payout in respect of the 2016 annual cash incentive plan. The fees paid to Willis Towers Watson for Remuneration Committee advice during 2017, charged on a time and expense basis, were £98,000 and the fee paid to Mercer was £4,350. Willis Towers Watson also provided other human resources and compensation advice to the Company for the level below the Board. Mercer also provided insurance broking, market data, actuarial and investment consulting services both at a global and local level. Both Willis Towers Watson and Mercer comply with the Code of Conduct in relation to Executive Remuneration Consulting in the United Kingdom and the Remuneration Committee is satisfied that their advice is objective and independent.

REMUNERATION IMPLEMENTATION REPORT

SINGLE TOTAL FIGURE ON REMUNERATION

The amounts for 2017 have been converted into US$ for ease of comparability using the exchange rates of £ to US$1.2877 and € to US$1.1279 (2016: £ to US$1.349 and € to US$1.106).

	Olivier Bohuon Appointed 1 April 2011		Graham Baker Appointed 1 March 2017	Julie Brown Appointed 4 February 2013 (resigned with effect from 11 January 20	
	2017	2016	2017	2017	2016
Fixed pay					
Base salary	$ 1,330,347	$ 1,295,017	$ 547,273	$ 21,606	$ 730,257
Payment in lieu of pension	$ 399,104	$ 388,505	$ 164,182	$ 6,482	$ 219,078
Taxable benefits	$ 177,433	$ 166,465	$ 22,308	$ 637	$ 30,007
Annual variable pay					
Annual Incentive Plan – cash	$ 1,208,911	$ 592,902	$ 683,797	–	–
Hybrid					
Annual Incentive Plan – equity	$ 665,173	$ 652,258	$ 361,200	–	–
Long-term variable pay					
Performance Share Plan	$ 1,251,957	$ 237,703	–	–	–
Total	$ 5,032,925	$ 3,332,850	$ 1,778,760	$ 28,725	$ 979,342

Base salary	the actual salary receivable for the year.
Payment in lieu of pension	the value of the salary supplement paid by the Company in lieu of a pension.
Taxable benefits	the gross value of all taxable benefits (or benefits that would be taxable in the UK) received in the year.
Annual Incentive Plan – cash	the value of the cash incentive payable for performance in respect of the relevant financial year.
Annual Incentive Plan – equity	the value of the equity element awarded in respect of performance in the relevant financial year, but subject to an ongoing performance test as described on pages 87-88 of this report.
Performance Share Plan	the value of shares vesting that were subject to performance over the three-year period ending on 31 December in the relevant financial year. For awards vesting in early 2018 this is based on an estimated share price of 1,352.140p per share, which was the average price of a share over the last quarter of 2017. The value of the 2014 share awards that vested in 2017 have now been restated with the share price on the date of actual vesting being 1,221.625p per share on 7 March 2017.
Total	the sum of the above elements.

All data is presented in our reporting currency of US$. Amounts for Olivier Bohuon have been converted from EURO and amounts for Julie Brown and Graham Baker from GBP using average exchange rates. Given currency volatility in 2017, this may give the impression of changes that are misleading. Data is presented in local currency in the subsequent sections in the interests of full transparency.

REMUNERATION IMPLEMENTATION REPORT

Retirement of Olivier Bohuon

On 9 October 2017, we announced that Olivier Bohuon intended to retire as Chief Executive Officer by the end of 2018.

Up until the date of his retirement, Olivier Bohuon will continue to be paid his salary, pension and benefits and will participate on a pro-rata basis in the 2018 Annual Incentive Plan, which will be delivered entirely as cash. He will not receive a Performance Share Plan in respect of 2018. In-line with good leaver provisions in the Plan Rules and Remuneration Policy, the awards granted under the Performance Share Plan in 2016 and 2017 (as detailed in this report) will be pro-rated for length of time held and will, subject to the performance conditions being satisfactorily met, vest on the original vesting dates on the third anniversary of the respective dates of grant. The 2017 award will remain subject to a two-year post-vesting holding period.

FIXED PAY

Base salary

In February 2017, it was agreed that with effect from 1 April 2017, Executive Directors would be paid the following base salaries.

	2017	2016
Olivier Bohuon	€1,179,490	€1,179,490
Graham Baker	£510,000	–

In February 2018, we reviewed the base salaries of the Executive Directors, having considered general economic conditions and average salary increases across the rest of the Group, which have averaged at 2% in the UK and the US; 2.6% globally. The Remuneration Committee has agreed that there will be no increase to the base salary of Olivier Bohuon and that Graham Baker’s salary will be increased by 2% to £520,200.

Payment in lieu of pension

In 2017, Olivier Bohuon, Graham Baker and Julie Brown until her resignation on 11 January 2017 received a salary supplement of 30% of their basic salary to apply towards their retirement savings, in lieu of membership of one of the Company's pension schemes.

Benefits

In 2017, Olivier Bohuon, Graham Baker and Julie Brown until her resignation on 11 January 2017 received death in service cover of seven-times basic salary, of which four-times salary is payable as a lump sum, with the balance used to provide for any spouse and dependent persons. They also received health cover for themselves and their families, a car allowance and financial consultancy advice. Olivier Bohuon also received assistance with travel costs between London and Paris. The same arrangements will apply in 2018 for Olivier Bohuon and for Graham Baker. The following table summarises the value of benefits on an element-by-element basis in respect of 2016 and 2017. Julie Brown received these benefits until she retired from the Board on 11 January 2017.

	Olivier Bohuon		Graham Baker		Julie Brown	
	2017	2016	2017	2016	2017	2016
Health cover	£17,807	£15,672	£1,217	–	£44	£1,440
Car and fuel allowance	£15,000	€18,292	£14,182	–	£451	£14,640
Financial consultancy advice	£34,204	£66,572	£1,925	–	–	£6,614
	€37,736	–	–	–	–	–
Travel costs	£33,703	£23,814	–	–	–	–
Subscriptions	£4,023	£2,344	–	–	–	–

ANNUAL VARIABLE PAY

Annual Incentive Plan 2017

Cash Element

During 2016, the Remuneration Committee reviewed the operation of the Annual Incentive Plan and the performance measures and weightings which would apply to the cash element of the Annual Incentive Plan. These changes placed a greater emphasis on financial goals reflecting the importance we place on achievement of financial measures. The financial measures comprise 75% of the total award and are split between revenue (35%), trading profit margin (25%), and trading cash flow (15%). These measures were selected because revenue and trading profit margin constitute the key drivers of profit growth, and trading cash flow was a key measure of how efficiently we turn our assets into cash. Trading profit margin is a critical measure both for the business and our investors and delivering margin improvements is a core commitment under our strategy.

The remaining 25% of the total award are individual business objectives, similar to previous years, tied to our strategic priorities. As in previous years, these business objectives fell into the categories of Business Process, People and Customer.

The weighting of the performance measures for 2017 can be summarised as follows:

Financial objectives	75%
Revenue	35%
Trading profit margin	25%
Trading cash flow	15%
Business objectives	25%
Business process	8.33%
People	8.33%
Customer	8.33%

The figures for threshold, target and maximum relating to the financial objectives of the cash element of the 2017 Annual Incentive Plan are shown below:

	Threshold	Target	Maximum	Actual
Revenue	$ 4,578 m	$ 4,720 m	$ 4,861 m	$ 4,654 m[1]
Trading profit margin	21.8 %	22.3 %	22.7 %	22.3 %[1]
Trading cash flow[2]	$ 801 m	$ 890 m	$ 979 m	$ 940 m

1 At constant exchange rates. See page 182.

2 During the year, the trading cash flow target was adjusted upwards to reflect the change regarding the cash funding of closed post-retirement benefit schemes (see pages 150–155).

'Target' was set and approved by the Board in the 2017 Budget. 'Threshold' and 'Maximum' are set at +/ 3% from the target for revenue, at +/ 45bps for the trading profit margin measure and at +/ 10% for the trading cash flow from target.

This resulted in a bonus achievement of 73% of salary in respect of the financial objectives.

	Weight		Achieved % of target		Award % of salary	
Revenue	35	%	77	%	26.9	%
Trading profit margin	25	%	107	%	26.8	%
Trading cash flow	15	%	128	%	19.2	%

Accordingly, the following amounts have been earned by Olivier Bohuon and Graham Baker under the cash element of the Annual Incentive Plan in respect of their financial objectives.

Olivier Bohuon €859,517
Graham Baker £371,647

The same measures and weightings will apply to the financial measurements of the cash element of the Annual Incentive Plan 2018. For reasons of commercial sensitivity, we are unable to disclose the precise targets now, but they will be disclosed in the 2018 Remuneration Report at the time of vesting.

Business Objectives

When setting business objectives for the upcoming year, the Board looks not only at the expected financial performance for the year, but also at the actions it expects the Executive Director to carry out in the year to build a solid foundation for financial performance over the longer term. In reviewing performance against these objectives at the end of the year, the Board is mindful that there is not always a necessary correlation between financial performance and the achievement of business objectives.

REMUNERATION IMPLEMENTATION REPORT

The table below sets out how Olivier Bohuon and Graham Baker have performed against the business objectives of People, Business Process and Customers.

Olivier Bohuon	Graham Baker
People	
– Delivered 50bps improvement in Group Great Place to Work Trust Index, meeting target of 67%.	– Delivered 30bps improvement Finance function Great Place to Work Trust Index, meeting target of 67%.
– Further five countries awarded Great Place to Work Accreditation, ahead of target of two new countries, with nine countries in total now recognised.	– Met target to upgrade Finance leadership team through combination of internal moves and external hires. Exceeded targets to retain and develop top Finance talent (80% of critical roles filled internally vs 50% target).
– Made progress against targets for 50% of critical roles filled by top talent (48% achieved); met target to identify internal successors for 50% of critical roles. Target to reduce voluntary turnover of top talent missed (12% against target of less than 10%).	Exceeded target on Finance leadership retention, with minimal loss of top talent against target of less than 10%.
– Clear communication of strategy and implementation plans across the Group through direct and indirect channels to drive alignment and increase engagement.	
– Target of delivering $5 million incremental revenue from commercial excellence programme not met with remediation action initiated.	
– Achieved target of all employees and third party sellers completing more than 95% of global compliance on time.	
Business Process	
	– Maintaining an effective financial control environment.

– Achieved target of new global R&D model fully operational by first quarter of 2017, including Portfolio Innovation Board to drive strategy and prioritise projects. More than 80% of programme milestones met tracking towards best-in-class standard of 90%, and programme to develop further clinical evidence progressing to plan.

– Met target to hold employees accountable for Finance policies and procedures, with 95% compliance on Minimum Acceptable Practices (MAPs) and deeper checking across all Group countries.

– Finance Transformation plan built, including integrating some back-office services into Global Business Services.

– First phase of new IT finance system successfully implemented in North America on time and within budget.

– Established relationships with investors and analysts supporting Group IR programme, receiving excellent feedback from external stakeholders.

Customers

– Met target to continue to develop new business models including mid-tier portfolio in the Emerging Markets and eCAP in the US.

– Roadmap for mid-tier product development completed in-line with target, with notable successes including ANTHEM Knee and ATLAS HF Nail in Emerging Markets. Mid-tier portfolio revenue growth tracked behind target.

– Met target to provide robust financial modelling to improve business decision making processes, including improved visibility of R&D portfolio value and completion of acquisition of Rotation Medical, Inc.

– Delivered leadership with Chief Executive Officer in developing APEX programme to improve competitiveness of Smith & Nephew.

– Met tax targets with tax on trading reduced from 23.8% in 2016 to 17.1% in 2017 reflecting one-off benefit following the conclusion of a US tax audit, further progress in improving our tax rate, tax provision releases following expiry of statute of limitations and a beneficial geographical mix of profits on trading.

This resulted in a bonus achievement of 18% of salary in respect of the business objectives.

	Weight	Achieved % of target	Award % of salary
People	8.33%	72%	6%
Business Process	8.33%	100%	8%
Customers	8.33%	50%	4%

Accordingly, the following amount has been earned by Olivier Bohuon under the cash element of the Annual Incentive Plan in respect of his business objectives.

Olivier Bohuon €212,308

This resulted in a bonus achievement of 31% of salary in respect of the business objectives.

	Weight	Achieved % of target	Award % of salary
People	8.33%	120%	10%
Business Process	8.33%	132%	11%
Customers	8.33%	120%	10%

Accordingly, the following amount has been earned by Graham Baker under the cash element of the Annual Incentive Plan in respect of his business objectives.

Graham Baker £159,375

The same measures and weightings will apply to the business objectives of the cash element of the Annual Incentive Plan in 2018.

HYBRID

Equity Incentive Award

The individual performance of all employees in the Group is assessed on two bases. The first looks at what has been achieved, namely the extent to which the employee has performed against the financial and business objectives set at the beginning of the year. The second looks at how this performance has been achieved, reflecting the right culture and values in accordance with our critical enablers. Against each, the employee is rated as having performed below, in-line or above expectations.

		Assessment of how Executive Directors have achieved		
		Below expectations	In-line with expectations	Above expectations
Assessment of what has been achieved	Below expectations	No Award	No Award	No Award
	In-line with expectations	No Award	Award of 50% of Salary	Award of 55% of Salary
	Above expectations	No Award	Award of 55% of Salary	Award of 65% of Salary

The Remuneration Committee has considered the performance of Olivier Bohuon and Graham Baker in exactly the same way as other employees in the Group when determining the level of Equity Incentive Award to be made to them. In assessing their performance against the same financial and business objectives used to determine the level of their cash award, the Remuneration Committee has determined that on the first criterion (assessing what they have achieved) Olivier Bohuon and Graham Baker have both performed in-line with expectations throughout the year. On the second criterion (assessing how they have achieved), the Remuneration Committee has determined that Olivier Bohuon has performed in-line with expectations and Graham Baker has performed above expectations. These ratings result in an Equity Incentive Award of 50% of salary for Olivier Bohuon and 55% of salary for Graham Baker.

In summary, as a result of the financial performance described on page 85 and the performance described in the table on page 86, the Remuneration Committee determined that the following awards be made under the Annual Incentive Plan in respect of performance in 2017:

	Cash Component		Equity Component	
Executive Director	% of salary	Amount	% of salary	Amount
Olivier Bohuon	91%	€1,071,825	50%	€589,745
Graham Baker	104%	£531,022	55%	£280,500

These figures are converted into dollars and included under Annual Incentive Plan (cash) and (equity) in the single figure table on page 83.

As a result of the 2017 performance assessment for Olivier Bohuon, the first tranche of the Equity Incentive Award made in 2017, the second tranche of the Equity Incentive Award made in 2016 and the third tranche of the Equity Incentive Award made in 2015 will vest. Both the grant and vesting of these awards are subject to Olivier's performance discussed on page 86. Graham Baker was not employed during 2016 and therefore received no Equity Incentive award in 2017.

Director	Date of Grant	Number of shares under award vesting	Number of shares to vest from each grant subject to performance
Olivier Bohuon	7 March 2017 – 1st tranche	13,886	27,779
	7 March 2016 – 2nd tranche	16,717	16,725
	9 March 2015 – 3rd tranche	12,849	0

REMUNERATION IMPLEMENTATION REPORT

Details of awards made under the Equity Incentive Programme during 2017

Details of conditional awards over shares, granted as part of the Annual Equity Incentive Programme to Executive Directors under the rules of the Global Share Plan 2010 for their 2016 performance (awarded in 2017) are shown below. The performance conditions and performance periods applying to these awards are detailed above.

Date granted	Number of shares under award	Date vesting
Olivier Bohuon		
7 March 2017	41,665	1/3 on 7 March 2018
		1/3 on 7 March 2019
		1/3 on 7 March 2020

The precise awards granted in 2018 to Olivier Bohuon and Graham Baker in respect of service in 2017 will be announced when the awards are made and will be disclosed in the 2018 Annual Report.

Olivier Bohuon has announced his intention to retire by the end of 2018 and will therefore not be entitled to receive an Equity Incentive Award in 2019 after ceasing to be an employee. He will therefore receive a cash amount equivalent to the Equity Incentive Award he would have received, if any, had he remained employed. This will be disclosed in full in the 2018 Remuneration Report.

The Equity Incentive Award element will operate in 2018 in exactly the same way as in 2017 and previous years. The Remuneration Committee will assess what has been achieved by the Executive Directors against the same financial and business objectives used to determine the level of their cash awards. The Remuneration Committee will assess how the Executive Directors have achieved their objectives by considering the role played by the Executive Directors in establishing an appropriate culture and set of values throughout the organisation. The level of Equity Incentive Award to be made will be determined according to the matrix on page 87.

LONG-TERM VARIABLE PAY

Performance Share Plan

Performance Share Programme – 2017 grants

Performance share awards granted in 2017 were made to Executive Directors under the Global Share Plan 2010 to a maximum value of 190% of salary (95% for target performance). During 2016, the Remuneration Committee reviewed the operation of the Performance Share Programme and made changes to the performance measures and weightings which were included with the Remuneration Policy and approved at the Annual General Meeting on 6 April 2017. The four equally weighted performance measures are relative TSR, return on invested capital, sales growth and cumulative free cash flow. These measures are aligned with our financial priorities and strategies. Performance will be measured over the three financial years from 1 January 2017 and awards will vest subject to performance and continued employment in 2020. Sufficient shares will be sold to cover taxation obligations and the Executive Directors will be required to hold the net shares for a further period of two years.

The two equally weighted peer groups against which the Company's TSR performance will be measured are defined at the start of each performance period based on constituents of the following:

– A sector-based peer group based on those companies classified as the S&P 1200 Global Healthcare subset comprising Medical Devices, equipment and supplies companies (official industry classifications of 'Health Care Equipment and Supplies, Life Sciences Tools & Services and Health Care Technology'). This is a broader sector-based peer group than in previous years, so that we maintain a focus on outperforming our broad sector without being impacted by the volatility of a smaller group.

– FTSE 100 constituents excluding financial services and commodities companies. This is in response to shareholders who assess our performance not based on sector, but instead based on the index we operate in.

The Group's TSR performance and its performance relative to the comparator group is independently monitored and reported to the Remuneration Committee by Willis Towers Watson.

Total Shareholder Return (TSR) performance is relative to two separate indices as follows:

	Award vesting as % of salary at date of grant	
Relative TSR ranking	Sector Based Peer Group	FTSE100 Peer Group
Below median	Nil	Nil
Median	5.9375%	5.9375%
Upper quartile or above	23.75%	23.75%

Awards will vest on a straight-line basis between these points. If the Company's TSR performance is below median, none of this part of the award will vest.

Return on invested capital (ROIC), adds focus on enhancing operating performance and reducing the under-performing asset base. 25% of the award will vest subject to ROIC:

ROIC will be defined as:

Net Operating Profit1 less Adjusted Taxes2
(Opening Net Operating Assets + Closing Net Operating Assets3)/2

ROIC will be measured each year of the three-year performance period and a simple average of the three years will be compared to the targets below (precise numbers will be included in the Remuneration Report prospectively). The Remuneration Committee will have the discretion to adjust ROIC targets in the case of significant events such as material mergers, acquisitions and disposals and that such adjustment will be consistent with the deal model and approved by the Board at the time of the transaction.

1 Operating profit is as disclosed in the Group income statement in the Annual Report.

2 Adjusted taxes represents our taxation charge per the Group income statement adjusted for the impact of tax on items not included in Operating Profit notably interest income and expense, other finance costs and share of results of associates.

3 Net Operating Assets comprises net assets from the Group balance sheet (Total assets less Total liabilities) excluding the following items: Investments, Investments in associates, Retirement benefit assets and liabilities, Long-term borrowings, Bank overdrafts and loans, and Cash at bank.

The awards subject to ROIC will vest as follows:

Return on Invested Capital	Award vesting as % of salary
Below Threshold 11.1%	Nil
Threshold 11.1% (1.9% of target)	11.875%
Target 13% (as derived from the Strategic Plan)	23.75%
Maximum or above 14.9% (+1.9% of target)	47.5%

Awards will vest on a straight-line basis between these points.

Sales growth focuses on growth in both Established Markets and Emerging Markets. 25% of the award will be subject to sales growth and will vest as follows:

Sales growth over three-year period commencing 1 January 2017	Award vesting as % of salary
Below Threshold	Nil
Threshold (3% of target)	11.875%
Target	23.75%
Maximum or above (+3% of target)	47.5%

It is not possible to disclose precise targets for sales growth as this will give commercially sensitive information to our competitors concerning our growth plans and is potentially price sensitive information. This target however will be disclosed in the 2019 Annual Report, when the Committee will discuss performance against the target.

Cumulative free cash flow is defined as net cash inflow from operating activities, less capital expenditure, less the cash flow input of certain adjusted items. Free cash flow is the most appropriate measure of cash flow performance because it relates to cash generated to finance additional investments in business opportunities, debt repayments and distribution to shareholders. This measure includes significant elements of operational financial performance and helps to align Executive Director awards with shareholder value creation.

It is important as it is derived from increased revenues and healthy trading profits. Having a healthy cash flow will enable us to continue to grow and invest. 25% of the award will be subject to cumulative free cash flow performance and will vest as follows:

Cumulative free cash flow	Award vesting as % of salary
Below $1,482m	Nil
$1,482m (13% of target)	11.875%
$1,703m	23.75%
$1,924m or more (+13% of target)	47.5%

REMUNERATION IMPLEMENTATION REPORT

Performance Share Programme 2018

A performance share award will be made in 2018 to Graham Baker under the Global Share Plan 2010 to a maximum value of 190% of salary (95% for target performance). No performance share award will be made to Olivier Bohuon in 2018.

Performance will be measured over the three financial years commencing 1 January 2018 against the same four equally weighted performance measures as in 2017: relative TSR, return on invested capital, sales growth and cumulative free cash flow. On vesting, sufficient shares will be sold to cover taxation obligations and Graham Baker will be required to hold the net shares for a further period of two years.

TSR performance will be measured in the same way as in 2017 as described on page 88 against the same two peer groups.

Return on invested capital (ROIC) will be measured in the same way as in 2017, as described on page 89. The targets will be as follows:

Return on Invested Capital	Award vesting as % of salary
Below Threshold 11.6%	Nil
Threshold 11.6% (1.25% of target)	11.875%
Target 12.9% (as derived from the Strategic Plan)	23.75%
Maximum or above 14.1% (+1.25% of target)	47.5%

Awards will vest on a straight-line basis between these points.

Sales growth will be measured in the same way as in 2017, as described on page 89. The targets will be as follows:

Sales growth over three-year period commencing 1 January 2018	Award vesting as % of salary
Below Threshold	Nil

Threshold (2.7% of target)	11.875%
Target	23.75%
Maximum or above (+2.7% of target)	47.5%

It is not possible to disclose precise targets for sales growth as this will give commercially sensitive information to our competitors concerning our growth plans and is potentially price sensitive information. This target however will be disclosed in the 2020 Annual Report, when the Committee will discuss performance against the target.

Cumulative free cash flow will be measured in the same way as in 2017, as described on page 89. The targets will be as follows:

Cumulative free cash flow	Award vesting as % of salary
Below $1,575m	Nil
$1,575m (13% of target)	11.875%
$1,810m	23.75%
$2,046m or more (+13% of target)	47.5%

VESTING OF AWARDS MADE IN 2015

Performance Share Programme 2015

Since the end of the year, the Remuneration Committee has reviewed the vesting of conditional awards made to Executive Directors under the Global Share Plan 2010 in 2015. Vesting of the conditional awards made in 2015 was subject to performance conditions based on TSR, revenue in Emerging Markets and cumulative free cash flow measured over a three-year period commencing 1 January 2015.

25% of the award was based on the Company's TSR relative to a bespoke group of 12 Medical Devices companies. This group comprised of the following companies: Baxter, Becton Dickinson, Boston Scientific, Coloplast, Conmed, Edwards Life Sciences, Medtronic, NuVasive, Orthofix, Stryker, Wright Medical and Zimmer. The following companies delisted during the period and were therefore removed: Covidien, C R Bard, Nobel Biocare and St Jude Medical. Against this peer group, the Company's TSR performance ranked below median meaning that this part of the award therefore vested at 0%.

25% of the award was based on revenues in Emerging Markets. The threshold set in 2015 was $2,395 million with a target of $2,818 million. Over the three-year period, the adjusted revenues in Emerging Markets were $2,411 million. These adjustments include translational foreign exchange and Board-approved M&A . This part of the award therefore vested at 13% out of the 25% target.

50% of the award was based on cumulative free cash flow performance. Over the three-year period, the adjusted cumulative free cash flow was $2,024 million which is between target and maximum. These adjustments include items such as Board-approved M&A, including the acquisition of BlueBelt and Board-approved Business Plans such as the metal-on-metal settlements. This part of the award therefore vested at 95%.

	Threshold	Target	Maximum	Actual	Percentage Vesting
TSR	Median	–	Upper Quartile	Below Median	0%
Emerging Markets Sales	$2,395m	$2,818m	$3,240m	$2,411m	13%
Cumulative Free Cash Flow	$1,578m	$1,814m	$2,050m	$2,024m	95%

Overall therefore, the conditional awards made in 2015 will vest at 54% of maximum (108% of target) on 9 March 2018 as follows:

Director	Date of grant	Number of shares under award at maximum	Number vesting
Olivier Bohuon	9 March 2015	133,156	71,904

DETAILS OF OUTSTANDING AWARDS MADE UNDER THE PERFORMANCE SHARE PROGRAMME

Details of conditional awards over shares granted to Executive Directors subject to performance conditions are shown below. These awards were granted under the Global Share Plan 2010. The performance conditions and performance periods applying to these awards are detailed on pages 88 and 89.

	Date granted	Number of ordinary shares under award at maximum	Date of vesting
Olivier Bohuon	9 March 2015	133,1561	9 March 2018
	7 March 2016	146,620	7 March 2019
	7 March 2017	158,328	7 March 2020
Graham Baker	7 March 2017	79,166	7 March 2020

1On 6 February 2018, 46% of the award granted at maximum to Olivier Bohuon lapsed following completion of the performance period.

SUMMARY OF SCHEME INTERESTS AWARDED DURING THE FINANCIAL YEAR

	Olivier Bohuon		Graham Baker1	
	Number of shares	Face value	Number of shares	Face value
Annual Equity Incentive Award (see page 87)	41,665	€589,745	–	–
Performance Share Award at maximum (see page 91)	158,328	€2,241,030	79,166	£969,000

1 Annual Equity Incentive Awards for 2017 were based on performance for 2016, hence Graham Baker received no award.

Please see Policy Table on pages 99 and 100 for details of how the above plans operate. The number of shares is calculated using the closing share price on the day before the grant, which for the awards granted on 7 March 2017 was 1,224p.

REMUNERATION IMPLEMENTATION REPORT

SINGLE TOTAL FIGURE ON REMUNERATION

Chairman and Non-Executive Directors

	Basic annual fee1		Committee Chairman / Senior Independent Director fee		Intercontinental travel fee		Total	
Director	2017	2016	2017	2016	2017	2016	2017	2016
Roberto Quarta	£ 412,000	£ 409,750	–	–	£ 7,000	£ 3,500	£ 419,000	£ 413
Vinita Bali2	£ 36,750	£ 63,000	–	–	£ 7,000	£ 21,000	£ 43,750	£ 84,0
	$ 59,780	$ 9,780			$ 21,000	–	$ 80,780	$ 9,78
Ian Barlow	£ 68,135	£ 68,135	£ 20,000	£ 18,750	£ 7,000	£ 3,500	£ 95,135	£ 90,3
Virginia Bottomley	£ 68,135	£ 68,135	–	–	£ 7,000	£ 3,500	£ 75,135	£ 71,6
Erik Engstrom	£ 68,135	£ 68,135	–	–	£ 7,000	£ 3,500	£ 75,135	£ 71,6
Robin Freestone	£ 68,135	£ 68,135	£ 16,667	–	£ 7,000	£ 3,500	£ 91,802	£ 71,6
Michael Friedman	$ 129,780	$ 129,780	$ 35,000	$ 33,000	$ 42,000	$ 35,000	$ 206,780	$ 197
Brian Larcombe3	£ 20,750	£ 68,135	£ 1,277	£ 18,750	–	£ 3,500	£ 22,027	