

SMITH & NEPHEW PLC
Form 20-F
March 04, 2019

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 20-F

INFORMATION FOR SHAREHOLDERS (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, 2018

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*
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*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: 887,952,258 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



Strategic report Smith & Nephew Annual Report 2018

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Our purpose

Physical health is never just about our body. It's our mind, feelings and ambitions. When something holds it back, it's our whole life on hold.

We're here to change that, to use technology to take the limits off living, and help other medical professionals do the same.

So that farmworkers, rugby players, grandmas and their grandkids stare down fear, see that anything's possible, then go on stronger. Inspired by a simple promise. Two words that bring together all we do...

Life Unlimited

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At a glance

Smith & Nephew is a leading portfolio medical technology company

OUR PURPOSE

Life Unlimited
Smith & Nephew exists to restore people’s bodies,
and their self-belief.

HIGHLIGHTS

REVENUE

\$4,904m

**REVENUE BY
GEOGRAPHY**

OUR CULTURE PILLARS

These guide our behaviours and build a winning
spirit.

EMPLOYEES

16,000+

YEARS

160+

United States \$2,354m
Other Established Markets \$1,693m
Emerging Markets \$857m

Care

A culture of empathy and understanding for each
other, our customers and patients

**COUNTRIES
SUPPORTING
HEALTHCARE
PROFESSIONALS**

100+

MANUFACTURING & QUALITY

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

Collaboration

A culture of teamwork based on mutual
trust and respect

Courage

A culture of continuous learning,
innovation and accountability

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OUR STRATEGIC IMPERATIVES

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

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1 Achieve the full potential of our portfolio

2 Transform the business through enabling
technologies

3 Expand in high-growth segments

4 Strengthen talent and capabilities

5 Become the best owner

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OUR GLOBAL FRANCHISE AREAS

ORTHOPAEDICS

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

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SPORTS MEDICINE & ENT

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

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ADVANCED WOUND MANAGEMENT

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

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OUR NEW COMMERCIAL STRUCTURE

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

INNOVATION

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

10% MORE INVESTED IN R&D IN 2018
\$246m

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Financial highlights

REVENUE

\$4,904m

Reported
+3%Underlying¹
+2%

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

REVENUE BY MARKET

Established Markets

\$4,047m
Reported
+2%Underlying¹

+1%

KPI

Emerging
Markets\$857m
Reported
+7%Underlying¹

+8%

DIVIDEND PER SHARE

36.0¢

+3%

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

OPERATING PROFIT

\$863m

KPI

8%

Operating profit margin of 17.6% is down 200bps year-on-year due to impact of restructuring charges.

EARNINGS PER SHARE (EPS)

76.0¢

13%

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

TRADING PROFIT¹

\$1,123m

KPI

+7%

Trading profit margin¹ was 22.9%, up 90bps year-on-year reflecting both improved trading performance and cost control and a 50bps one-off legal settlement benefit.

ADJUSTED EARNINGS PER SHARE¹ (EPSA)

100.9¢

+7%

The increase reflects improved trading performance and lower tax rate on trading.¹

R&D EXPENDITURE

\$246m

KPI

+10%

R&D expenditure was up 10% reflecting our increased investment in new products and clinical evidence.

RETURN ON INVESTED CAPITAL¹ (ROIC)

12.5%

180bps

The decrease reflects primarily the fall in operating profit.

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

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

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

Roberto Quarta

Chair

DEAR SHAREHOLDER

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

CHIEF EXECUTIVE OFFICER

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

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

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

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

LEADERSHIP & CULTURE

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

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

STRATEGY

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

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

2018 PERFORMANCE

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

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

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

BOARD CHANGES

During 2018, we welcomed Roland Diggelmann as a Non-Executive Director. Roland was, until recently, Chief Executive Officer of Roche Diagnostics and a member of the Corporate Executive Committee of F. Hoffmann-La Roche Ltd. He brings direct experience in orthopaedics from previous senior roles at Zimmer.

Ian Barlow will step down from the Board at the Annual General Meeting in April 2019, having completed a nine-year term. Ian has served Smith & Nephew with great distinction as our Senior Independent Director, and

previously as Chair of the Audit Committee. I have been grateful for his counsel and thank him for his significant contribution over the years.

Michael Friedman, Chair of our Compliance & Culture Committee, will also be retiring at that time after six years' service, and I thank him for his leadership in this crucial area. Robin Freestone will replace Ian as Senior Independent Director and Marc Owen will replace Michael as Chair of the extended Compliance & Culture Committee.

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

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

Yours sincerely,

Roberto Quarta

Chair

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Chief Executive Officer's review

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

DEAR SHAREHOLDER

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

CREATING A PURPOSE-DRIVEN CULTURE

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

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

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

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

OUR BUSINESS AND STRATEGIC IMPERATIVES

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

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

- 1 Achieve the full potential of our portfolio
- 2 Transform the business through enabling technologies

3 Expand in high-growth segments

4 Strengthen talent and capabilities

5 Become the best owner

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

INCREASING CUSTOMER CENTRICITY

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

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

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

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

Namal Nawana

Chief Executive Officer

ADDING VALUE THROUGH ACQUISITIONS

Smith & Nephew completed 2018 with a net debt¹ to adjusted EBITDA ratio² of 0.8x and, with strong cash flows and cash conversion, we will look to appropriately deploy capital to M&A initiatives more significantly than in recent years as part of our business model for success.

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

In December, we announced the acquisition of Ceterix Orthopaedics, the developer of the NovoStitch™ Pro Meniscal Repair System. This product is highly complementary to our portfolio and will significantly expand our opportunity in the underserved meniscal repair segment.

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

2018 RESULTS

In 2018, revenue growth was 3% on a reported basis and 2% underlying, and we delivered a meaningful improvement in trading profit margin.

Geographically, we continued to build upon our strong position in the Emerging Markets, which now account for 17% of Group revenue. A solid performance in the US, our largest market, was somewhat offset by continued weakness in some European markets.

At a franchise level, highlights included the market beating growth from Knee Implants, the strong return to growth delivered in Hip Implants, and the increased adoption of our NAVIO robotics platform. Growth from our Advanced Wound Devices franchise also stood out, driven by our PICO single-use Negative Pressure Wound Therapy system.

Actions are underway to improve weaker performances from Arthroscopic Enabling Technology and Advanced Wound Bioactives.

After a slow start to 2018, it's pleasing that our team accelerated performance as the year progressed, whilst at the same time making the important changes to how we run the Company.

FOCUSED ON DELIVERY

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

We start 2019 with a new executive leadership team and operating structure in place. We have clarified our brand purpose with Life Unlimited and have introduced new culture pillars and strategic imperatives to support it.

Together, we are confident that we are building the right foundation for sustainable success and an ability to grow consistently with our markets in the future. This confidence is reflected in our financial guidance for further improvements in both revenue and margin performance in 2019, explained in detail by our Chief Financial Officer, Graham Baker, on page 37 of this Annual Report.

There is much to do to achieve our goals and aspirations but we are grateful for the opportunity to positively affect the patients, practitioners and health systems that we serve globally. I look forward to updating you on our progress.

Yours sincerely,

Namal Nawana

Chief Executive Officer

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

A successful business needs to have a purpose-driven culture

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

Namal Nawana

Chief Executive Officer

Life Unlimited

CARE

A culture of empathy and understanding for each other, our customers and patients

– We step into our customers' shoes, anticipate their needs and deliver the highest levels of innovation and service

– We strive to have the best understanding of the patients whom we ultimately serve, and we develop our products with them in mind

– Our passion for what we do drives us to continuously improve and expand the positive impact that we have on the world

COLLABORATION

A culture of teamwork, based on mutual trust and respect

– We are stronger, and achieve more, as a team. By joining forces we are both unstoppable and efficient

– Through transparent and respectful communication, we are motivated by a shared purpose and understand the impact of our individual contributions on our collective goals

– By encouraging different perspectives and leveraging our global experiences, we achieve the best outcomes

COURAGE

A culture of continuous learning, innovation and accountability

– By staying curious, thinking big and having the humility to challenge our conventional ways of thinking, we push the boundaries of our industry

– Fostering an entrepreneurial, can-do attitude we look for solutions and achieve them through talent and force of will

– With a growth mindset, we have the capability and confidence to win, and we do so with integrity and the highest ethical standards

Our strategic imperatives

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

GROW

Achieve the full potential of our portfolio

- 1 Improving execution to accelerate organic performance with a focus on (i) platform-specific plans, (ii) Ambulatory Surgery Centres and (iii) Emerging Markets, especially China and Latin America.

Transform the business through enabling technologies

- 2 By acquiring and developing leading enabling technologies to transform procedures, including robotics, imaging and augmented reality.

Expand in high-growth segments

- 3 By accelerating portfolio growth, strengthening or establishing leadership positions, and driving meaningful synergies.

TOGETHER

Strengthen talent and capabilities

- 4 By developing a winning culture to improve retention and attract talent.

EFFECTIVELY

Become the best owner

- 5 To drive meaningful margin expansion through operational transformation and organisation simplification.

MEASURING PERFORMANCE

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

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

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

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

Our markets

Competing in large, attractive markets

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

The medical devices and supplies segment of healthcare is today worth more than \$400 billion per annum. Within that, Smith & Nephew's product segments are worth approximately \$38 billion, growing at around 4% annually.

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

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

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

COMPLIANCE

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

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

GEO-POLITICAL FACTORS

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

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

A HIGHLY REGULATED INDUSTRY

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

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

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

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

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

* Source: Deloitte 2019 Global Health Care Outlook.

EVOLVING MODELS OF HEALTHCARE

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

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

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

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

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

SEASONALITY

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

comes at a lower cost, which may encourage some to schedule any required treatments or procedures in the final months of any given year.

COMPETITION

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

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

against Stryker and Depuy Synthes.

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

MARKET SIZE1
ORTHOPAEDICS

SPORTS MEDICINE2

ADVANCED WOUND
MANAGEMENT

Hip & Knee Implants

Trauma &
Extremities

\$5.0bn +5%

\$9.0bn +5%

\$14.5bn +2%

\$6.0bn +4%

A SMITH & NEPHEW 12%
B ZIMMER 33%
BIOMET

A SMITH & NEPHEW 8%
B DEPUY 43%
SYNTHESES3

A SMITH & NEPHEW 26%
B ARTHREX11%

A SMITH & NEPHEW 44%
B ACELITY 16%

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C	STRYKER	21%	C	STRYKER	26%	C	STRYKER	5%	C	MOLNLYCKE	10%
D	DEPUY	20%	D	ZIMMER	11%	D	DEPUY	12%	D	CONVATEC	7%
E	SYNTHES	3%	E	BIOMET	12%	E	SYNTHES	3%	E	OTHERS	53%
E	OTHERS	14%	E	OTHERS	12%	E	OTHERS	16%	E	OTHERS	53%

1Data used in 2018 estimates generated by Smith & Nephew is based on publicly available sources and internal analysis and represents an indication of market shares and sizes.

2Representing repair products and arthroscopic enabling technologies, and excluding ENT.

3A division of Johnson & Johnson.

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Our business model

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

OUR RESOURCES	CREATING VALUE THROUGH	
<p>Our people & culture</p> <p>Attracting, developing and retaining the best employees is important. We strive to build a purpose-driven culture based on strong and authentic values.</p>	<p>Purpose-driven culture</p> <p>We believe in Life Unlimited, and have three culture pillars that guide our behaviours and build a winning team spirit: Care, Collaboration and Courage.</p>	<p>Strategic imperatives</p> <p>Our five new strategic imperatives reflect our ambition to maximise commercial advantage from our marketplace. They will form our value creation plan for the medium term.</p>
<p>Ethics & compliance</p> <p>Committed to doing business the right way, applying strict principles to the way we work.</p>	<p>Strong product portfolio</p> <p>We have market-leading technology across our broad range of products. We deploy our capital to drive continued innovation from our R&D programmes and invest in product and technology acquisitions, which improve outcomes and widen access to life-changing care.</p>	<p>Life</p> <p>Unlimited</p> <p>Customer centricity</p> <p>Serving our customers is at the heart of our model. We have a global franchise model led by management who are specialists in their markets. This keeps us close to our customers, ensuring we can anticipate and meet their needs.</p>
<p>Sales & marketing</p> <p>Supporting customers through highly specialised sales teams with in-depth technical knowledge that surgeons and</p>		

nurses greatly
value.

Manufacturing &
quality

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

Medical
education

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

Research &
development

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

Sustainability

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

OUR
RESOURCES

OUR CULTURE PILLARS

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OUR STRATEGIC
IMPERATIVES

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VALUE DELIVERED IN 2018		VALUE SHARED
REVENUE		Shareholders
\$4,904m		We have a progressive dividend policy and in respect of 2018 our shareholders benefited from a 3% increase in dividend. In addition, our shares rose 14% over the course of 2018.
OPERATING PROFIT	TRADING PROFIT ¹	
\$863m	\$1,123m	
DIVIDEND	JOBS	Patients
\$321m	16,000+	Patients in more than 100 countries were treated with our products in 2018. We continued to widen access to our products, with 17% of revenue now coming from sales to the emerging markets.
EFFICIENCY SAVINGS	PUBLISHED CLINICAL EVIDENCE	
\$60m	200+	
PRACTITIONER TRAINING INSTANCES	PHILANTHROPIC DONATIONS	Customers
50,000+	\$8m	We continued to expand treatment options available through R&D and acquisitions, published more than 200 pieces of clinical or economic evidence, and provided extensive professional development training.
1 These non-IFRS financial measures are explained and reconciled to the most directly comparable financial measure prepared in accordance with IFRS on pages 194–198.		Employees
		6,000 employees engaged in the development of our new purpose and culture pillars which are guiding revised evaluation, diversity and development programmes.
		Communities
		We work in a sustainable, ethical and responsible manner, making \$8m in cash and product donations in 2018.

OUR FRANCHISES
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OUR RESULTS
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OUR RESOURCES
PAGE 4

Our franchises

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

Orthopaedics

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

Sports Medicine & ENT

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

Advanced Wound Management

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

<p>1 Smith & Nephew’s range of products for specialised knee replacement procedures include leading products for total, partial and patellofemoral joint resurfacing procedures. Customers and patients benefit from our unique technologies including our proprietary advanced bearing surface, VERILAST™, our robotics-assisted platform, NAVIO™ Surgical System, and our customised VISIONAIRE™ Patient-Matched Instrumentation.</p>	<p>11</p> <p>12 20 flexibility and confidence utilising real-time imaging (without the need for a preoperative CT scan), hand-held robotics, a portable cart, and multiple partial and total knee implant options in an economically sound platform.²¹ NAVIO offers both partial and total knee options that include the first and only robotics-assisted bi-cruciate retaining knee procedure commercially available today.</p>	<p>1</p> <p>23</p>
<p>2 8 The range includes bi-cruciate stabilised and cruciate retaining options, and the JOURNEY II XR, an innovative bi-cruciate retaining knee implant launched in 2018, which is designed to retain the anterior and posterior cruciate ligaments (ACL/PCL) and deliver normal perception of movement and muscle control.⁹</p>		

Orthopaedics

Proven products to enhance quality of life

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

With best-in-class products utilising unique materials and backed by strong data, our Orthopaedics franchise is well-positioned for further growth.

Skip Kiil

KNEE IMPLANTS

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

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

The LEGION™/GENESIS™ II Total Knee System is a comprehensive system designed to allow surgeons to address a wide range of knee procedures. It includes the LEGION Revision Knee System, designed to offer surgeons improved options to deal with the complexities associated with revision knee arthroplasty.

These systems feature VERILAST Technology, our advanced bearing surface of OXINIUM™ Oxidized Zirconium with highly cross-linked polyethylene. The LEGION Primary Knee with VERILAST Technology has been laboratory-tested for 45 million cycles of wear simulation, approximating 30 years of activity. While lab testing is not the same as clinical performance, the tests showed significant reduction in wear compared to conventional technologies.^{10*}

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

The NAVIO Surgical System provides accuracy,¹² flexibility and confidence utilising real-time imaging (without the need for a preoperative CT scan), hand-held robotics, a portable cart, and multiple partial and total knee implant options in an economically sound platform.²¹ NAVIO offers both partial and total knee options that include the first and only robotics-assisted bi-cruciate retaining knee procedure commercially available today.

Additionally, our knee systems can utilise our VISIONAIRE Patient-Matched Instrumentation, whereby an MRI and X-Rays are used to create customised cutting guides designed to allow the surgeon to achieve optimal alignment of the new implant.²²

HIP IMPLANTS

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

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

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OUR FRANCHISES continued

Smith & Nephew's portfolio also includes the REDAPT™ Revision Hip System. The need to perform a revision can occur for a variety of reasons including infection, dislocation, or failure of the implants to achieve biologic fixation. REDAPT is designed to turn such complex hip revisions into efficient, reproducible surgeries, allowing surgeons to effectively recreate a patient's unique functionality, while quickly and easily addressing issues such as poor bone quality.²³

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

TRAUMA

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

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

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

OUR PERFORMANCE IN 2018

	Revenue	Reported growth	Underlying growth**
Knee Implants	\$1,017m	3%	3%
Hip Implants	\$613m	2%	2%
Trauma	\$493m	0%	1%

In Knee Implants we delivered a market beating growth in 2018. This was driven by double-digit underlying growth across our JOURNEY II Total Knee System, LEGION Revision Knee System and ANTHEM Knee System for the Emerging Markets.

In Hip Implants, performance improved markedly in the second half of the year, with improved execution driving demand for the POLAR3 total hip solution, with its class-leading survivorship data, and the continued roll-out of the REDAPT Revision System.

In Trauma we delivered good growth from INTERTAN Nails and drove an increasing contribution from the new EVOS SMALL plating system, offset by reduced tender activity in the Middle East.

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

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

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POLAR3 TOTAL HIP SOLUTION

The POLARSTEM and R3 Total Hip Solution has the best survivorship figures of any total hip construct at seven years according to the world's largest national joint registry.²⁶

OUR FRANCHISES continued

Sports Medicine & ENT

Technology to improve healthcare

We have a leading portfolio of instruments and implants for soft tissue repair, and a proud history of successfully addressing unmet clinical needs.

Brad Cannon

President of Sports Medicine & ENT

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

REGENETEN BIOINDUCTIVE IMPLANT

SPORTS MEDICINE JOINT REPAIR

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

Rotator cuff disease is a significant and costly problem^{3,16,17} that causes ongoing pain and limits patients’

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

mobility.¹⁸ The REGENETEN Bioinductive Implant

other existing products from the Smith & Nephew portfolio in a single procedure, significantly expanding the breadth of our comprehensive solutions for shoulder repair.

Enhancing our RCR portfolio, the REGENETEN™ Bioinductive Implant, acquired in 2017, is a breakthrough technology and technique that balances biomechanics and biology to enhance the body's natural healing response, helping tendons heal by inducing growth of new tendon-like tissue.^{1 3}

stimulates the body's natural healing response to support new tendon growth and disrupt disease progression.^{3,19}

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

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

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

The Smith & Nephew joint repair portfolio includes implants made from a variety of biocompatible materials, including next-generation anchors made of soft, all-suture material and REGENESORB™, an advanced biocomposite. For example, the Q-FIX All-Suture Anchor is ideal for a variety of arthroscopic shoulder and hip repairs, offering fixation performance superior to commonly used all-suture anchors and traditional anchors.⁴ The SUTUREFIX ULTRA All-Suture Anchor is an attractive option for procedures in which anatomic space is very limited⁵, while still delivering high fixation strength.⁶ Implants made from REGENESORB, including versions of the HEALICOIL™ Suture Anchor for shoulder repair and BIOSURE™ Interference Screw for knee repair, have been shown to be absorbed and replaced by bone within 24 months in pre-clinical studies.⁷ *

ARTHROSCOPIC ENABLING TECHNOLOGIES (AET)

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

The WEREWOLF™ and QUANTUM 2™ COBLATION™ Controllers, which are used with a wide range of high performance COBLATION radio frequency (RF) wands, enable surgeons to remove soft tissue precisely⁸ and control bleeding in a variety of arthroscopic procedures. WEREWOLF, our latest advance in COBLATION™ Technology, and the FLOW 50™ Wand have demonstrated faster patient recovery⁹ and better long-term patient outcomes^{10,11} and safety^{12,13} in knee procedures.* The WEREWOLF and QUANTUM 2 Controllers and their associated wands carry broad indications across Sports Medicine.

The LENS™ Integrated Visualisation System provides outstanding image quality and functionality in a simple three-in-one console (CCU, LED Light Source and Image Management System), camera head and iPad application. Our DYONICS™ shaver blades provide superior resection due to their sharpness and reduced clogging with their debris evacuation capabilities.¹⁴ GoFLO™ and Double® Pump Fluid Management Systems facilitate surgical access by expanding the joint space, providing haemostasis, and maintaining the saline environment necessary to perform arthroscopic procedures.

EAR, NOSE & THROAT (ENT)

In ENT, our COBLATION Technology has been used to remove tonsils and adenoids for over 15 years and is preferred by surgeons and patients for its ability to remove tissue at low temperatures with minimal damage to surrounding tissue. COBLATION Technology is also marketed for use in turbinate and laryngeal procedures.

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

OUR PERFORMANCE IN 2018

	Revenue	Reported growth	Underlying growth**
Sports Medicine Joint Repair	\$697m	11%	8%
AET	\$600m	2%	3%
Other Surgical Business***	\$209m	10%	10%

In 2018, strong growth in Sports Medicine Joint Repair franchise was driven by our shoulder repair portfolio. Within this, the recently acquired REGENETEN™ Bioinductive Implant for rotator cuff repair delivered more than 130% growth, performing ahead of expectations.

AET performance was held back by continued softness in mechanical and legacy radio-frequency resection. We expect the launch of the FLOW 90™ COBLATION™ wand for shoulder in the first half of 2019 to support better growth.

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

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* FDA cleared for use in the knee on all soft tissue types.

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

*** Includes ENT and NAVIO robotics system.

OUR FRANCHISES continued

Advanced Wound Management

Reducing the burden of wounds

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

Our customers choose the breadth and depth of our portfolio, innovation, and expertise in order to achieve their 'CLOSER TO ZERO' goals.

Simon Fraser

President of
Advanced
Wound Management

ADVANCED WOUND MANAGEMENT

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

T.I.M.E. stands for Tissue non-viable, Infection and/or Inflammation, Moisture imbalance, and Edge of wound non-advancing. These represent critical barriers of wound healing. T.I.M.E. was first established as a concept for best practice wound management in 2003¹ by a panel of world leading experts, and has since been widely adopted around the world, becoming a staple reference framework for routine clinical practice.²

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

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

ADVANCED WOUND CARE (AWC)

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

In infection management, our silver-based dressings (ACTICOAT™, DURAFIBER Ag™ and ALLEVYN™ Ag) provide clinicians with a range of solutions to address individual patient needs in managing wound infection. ACTICOAT, for instance, is a fast-acting, highly effective antimicrobial³ for serious infection on a wide range of wounds. Our Cadexomer iodine based IODOSORB™ dressing is indicated outside the US to deliver best in class efficacy effective against biofilms across numerous clinically relevant in vitro tests,⁴ animal biofilm models⁴ and in clinical practice.⁵

In exudate (or moisture) management our products are designed to respond to varying levels of wound exudate providing appropriate wound fluid absorption, lock in and evaporation properties to promote an optimal wound healing environment. This helps patients get on with their lives as well as lowering costs for materials and nursing time by reducing unnecessary dressing changes. Our key growth brand in this space is the ALLEVYN range with two focus variants, ALLEVYN Gentle Border dressing (versatile and adaptable, so suitable for a wide variety of chronic and acute wounds^{6,7}) and ALLEVYN LIFE dressing (our most advanced dressing, uniquely differentiated by its distinct quadrilobe shape which lasts for up to two times longer than any other dressing⁸). The ALLEVYN range was extended in 2018 through the launch of ALLEVYN LIFE Non Bordered to ensure the portfolio continues to meet broad needs.

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

ADVANCED WOUND BIOACTIVES (AWB)

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

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

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

Our most significant product by sales in this segment is SANTYL Ointment⁹, the only FDA-approved biologic enzymatic debriding agent for chronic dermal ulcers and severe burns. SANTYL plays an integral role in debriding chronic dermal ulcers and severely burned areas.

PICO 7

The UK's National Institute for Health and Care Excellence (NICE) issued a Medtech innovation briefing²⁶ on the prophylactic use of PICO which highlighted its potential to be more effective at preventing surgical site infections than standard surgical dressings. This is the only such briefing published by NICE on an NPWT device for preventing such complications.

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OUR FRANCHISES continued

ADVANCED WOUND DEVICES (AWD)

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

In the NPWT segment, the PICO™ Single Use Negative Pressure Wound Therapy System (sNPWT) brings the effectiveness of traditional NPWT in a modern, small portable system.¹⁰ It is designed for both open wounds and closed incisions, and leverages our proprietary AIRLOCK™ dressing technology.

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

PICO 7 delivers a more efficient vacuum and superior leak management than the previous version¹¹, includes an industry-first dressing-full indicator, which is intended to help reduce unnecessary dressing changes and wastage, and is over 25% quieter than the previous version.¹²

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

The PICO evidence base continued to grow, validating the patient and provider benefits of the technology, with the publication of key studies in multiple indications including orthopaedics, vascular, plastics, OBGYN, breast reconstruction and chronic wounds.^{13 24}

With RENASYS™ NPWT system, our strategy is to simplify the delivery of NPWT, combining the advantages of PICO with the simplicity and power of RENASYS TOUCH, an intuitive touchscreen traditional NPWT device delivering advanced features to manage large, highly exuding wounds.^{23,24}

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.²⁵

OUR PERFORMANCE IN 2018

	Revenue	Reported	Underlying
		growth	growth*
Advanced Wound Care	\$740m	3%	1%
Advanced Wound Bioactives	\$320m	6%	6%
Advanced Wound Devices	\$215m	10%	9%

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

In Advanced Wound Bioactives, performance from SANTYL, our largest product, was weaker than the previous year as volumes came under pressure. Following review of two large safety studies, the FDA approved the removal of the

boxed warning from REGRANEX, and we will relaunch this product in early 2019.

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

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

Our resources

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

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OUR RESOURCES

Our people & culture

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

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

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

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

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

CARE

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

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

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

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

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

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

culture pillars and replace our previous core competencies.

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

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

COLLABORATION

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

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

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

We are committed to employment practices based on equal opportunities, regardless of colour, creed, race, national origin, sex, age, marital status, sexual orientation, or physical or intellectual disability. We believe a person’s ability to perform essential functions of a job is the only relevant criteria.

In 2018, an internal evaluation showed that those teams with greater diversity achieved better results. The work also revealed that our people understand why valuing difference is important and our teams benefit from high levels of trust and respect.

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

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

COURAGE

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

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

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

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

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

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

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

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

NUMBER OF EMPLOYEES¹ 2018

Total employees	Senior managers ² and above	Board of Directors
16,377	788	12
Male 58%	Female 42%	Male 73%
Female 27%	Male 75%	Female 25%

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

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

OUR RESOURCES continued

Ethics & compliance

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

CODE OF CONDUCT AND BUSINESS PRINCIPLES

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

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

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

GLOBAL COMPLIANCE PROGRAMME

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

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

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

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

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

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

We constantly seek new ways to enhance our Compliance Programme. New measures in 2018 included expanding the compliance ambassador process where selected sales staff serve as compliance contact for their peers for some

training and questions, successfully completing a pilot for an enhanced root cause analysis methodology for recurring issues and implementing additional processes and training on data privacy.

AN ETHICAL EMPLOYER

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

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

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

Sales & marketing

We put customers at the heart of our commercial model

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

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

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

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

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

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

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

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

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

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

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

OUR RESOURCES continued

Manufacturing & quality

Efficiently delivering products of the highest quality

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

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

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

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

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

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

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

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

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

QUALITY AND REGULATORY AFFAIRS

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

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

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

Medical education

Supporting the safe and effective use of our products

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

3D PRINTING OF REDAPTCUPS IN MEMPHIS
 Additive manufacturing (AM), commonly referred to as 3D printing, is a novel manufacturing method that involves the use of a laser or electron beam, for example, to sinter polymer or metal powders into a solid part that is built layer by-layer. The REDAPT Revision Femoral System includes a Fully Porous Acetabular Cup featuring Smith & Nephew's unique CONCELOC Advanced Porous Titanium. This mimics the structure of cancellous bone, allowing ingrowth for improved fixation and stability.

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

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

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

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

ECC ENDORSED BY ROYAL COLLEGE OF SURGEONS

In 2018, Smith & Nephew's Expert Connect Centre (ECC) in Watford, UK became the first commercial surgical training facility in Europe to be accredited by the Royal College of Surgeons. The recognition

enables delegates to receive Continuing Professional Development (CPD) points when attending Smith & Nephew sessions, demonstrating their commitment to developing their surgical skills.

OUR RESOURCES continued

Research & development

We are increasing our investment in new products

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

Innovation is the lifeblood of our Company. We strive to partner with our customers to create meaningful solutions for unmet needs, with the goal of improving outcomes.

Vasant Padmanabhan

President of Research & Development

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

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

OUR ENTERPRISE R&D OPERATING MODEL

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

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

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

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

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

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

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

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

TREATING DIFFICULT REVISIONS

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

WIDENING OUR PORTFOLIO

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

WORLD FIRST

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

EXPANSIVE, USER FRIENDLY SYSTEM

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

Sustainability

Sustainability is better business

SUSTAINABILITY IS AT THE CORE OF THE BUSINESS

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

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

GROUP SUSTAINABILITY STRATEGY

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

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

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

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

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

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

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;

Implement the most sustainable product options.

SUSTAINABILITY VISION AND MISSION

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

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

Satisfy unmet health needs and promote greater access to treatment;

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

Prioritise materials that are reused, remanufactured or recycled;

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

Use natural resources efficiently;

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

Implement the most sustainable product options.

OUR PERFORMANCE

Our 10 long-term aspirational goals

2020 target

ZERO WORK-RELATED INJURIES AND ILLNESSES ACROSS THE VALUE CHAIN

10% reduction in Total Injury Rate (TIR) from 2016 actual.

Performance to 31 December 2018

13% reduction achieved (2016 TIR = 0.52, 2018 TIR = 0.45).

WATER: Total water impacts of products and solutions balanced with local human and ecosystem needs.

Water footprint available for products accounting for 75% of revenue and considerations embedded in new product development process. Total potable water consumption no higher than 2016 actual.

Water reduction of 21% achieved since 2016. Products and tools identified as per target. Life cycle assessment for a representative product underway with completion expected early 2019.

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 and 80% or more of waste generated reused, recycled or recovered.

79% of our total waste reused, recycled or energy recovered from, up from 74% in 2016. Products and tools identified as per target. Life cycle assessment underway.

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.

Products and tools identified as per target. Life cycle assessment underway.

Total Scope 1 & 2 greenhouse gas emissions reduced by 10% from 2016 actual.

16% reduction in emissions since 2016.

ETHICAL BUSINESS PRACTICES: All activities 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 identified and assessment to applicable ILO conventions completed for internal operations. Engagement with upstream suppliers and downstream distributors and agents initiated.

ZERO PRODUCT-RELATED AND SERVICE-RELATED PATIENT INJURIES

Robust system in place to detect, record, investigate and eliminate root cause of product and service-related patient injuries.

Systems in place.

Data being used to craft models to identify at-risk attributes.

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.

Social responsibility strategy in place. Alignment to new strategic imperatives under way.

PRODUCTS AND SERVICES are aligned to market economic, social and environmental expectations and anticipate future market conditions.

Sustainability attributes described for products accounting for 75% of revenue. Robust emphasis on sustainability attributes of new products/services in place.

Products identified and sustainability attributes agreed. New product development (NPD) sustainability focus

planning under way.
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 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 2019.

ENVIRONMENTAL, SOCIAL, AND ECONOMIC impacts of business activities fully understood and appropriately balanced.

Formal programmes in place to measure/assess the economic, social and environmental impacts of (1) potential acquisitions, (2) technologies to be extended to Emerging Markets, (3) innovative business models, (4) cost-of-quality reduction initiatives, and (5) manufacturing siting, functional optimisation and site utilisation alternatives.

Launched Enterprise Risk Management Policy and Manual and provided training in risk identification and mitigation.

SUSTAINABILITY continued

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

EMPLOYEE SAFETY, WELLNESS AND VOLUNTEERING

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

Engagement with the communities in which we operate continues to broaden and deepen through the active attention of site leadership, empowerment of local camaraderie councils as well as broader application of company-paid volunteering allowance and company matching of 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

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

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

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

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

CO₂e REPORTING METHODOLOGY, MATERIALITY AND SCOPE

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

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

	2018	2017	2016
CO ₂ e emissions (tonnes) from:			
Direct emissions	9,956	9,451	9,822
Indirect emissions	67,886	76,107	82,415
Total	77,842	85,558	92,237
Intensity ratio			
CO ₂ e (t) per \$m sales revenue	15.9	17.8	19.6
CO ₂ e (t) per full-time employee	4.7	5.2	5.9

Revenue: 2018: \$4.9bn; 2017: \$4.8bn; 2016: \$4.7bn. Full-time employee data: 2018: 16,681; 2017: 16,333; 2016: 15,584.

We report our emissions in two ‘scopes’.

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

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

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

Our performance

We improved performance, delivered meaningful efficiency savings, and generated good cash flow

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Chief Financial Officer's Review

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

DEAR SHAREHOLDER

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

2018 PERFORMANCE

Group revenue in 2018 was \$4,904 million, an increase of 3% on a reported basis and 2% on an underlying basis.¹ Our performance accelerated across the year, with 3% revenue growth on an underlying basis¹ in the second half, and we take good momentum into 2019.

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

Trading profit¹ for the year was \$1,123 million and the trading profit margin was up 90bps to 22.9%. This reflects both the 50bps benefit of a one-off legal settlement and improved trading performance and cost control.

The reported tax rate was 15.1% (2017: 12.7%). The tax rate on trading results¹ for the year to 31 December 2018 was 16.1% (2017: 17.1%). This was lower than the guided rate of between 20–21% mainly due to a one-off benefit from a tax provision release following expiry of statute of limitations and a beneficial geographical mix of profits.

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

Basic earnings per share ('EPS') was down 13% to 76.0¢, also primarily due to APEX restructuring charges. Adjusted earnings per share¹ ('EPSA') was up 7% at 100.9¢, reflecting the legal settlement gain, improved trading performance and the lower tax rate on trading results.

I'm pleased to report that trading cash flow¹ was \$951 million, up from \$940 million in 2017, and we had another year of strong cash conversion (as defined on page 195) at 85% (2017: 90%). Return On Invested Capital (ROIC¹ – as defined on page 198) was 12.5% (2017: 14.3%), reflecting the reduction in operating profit over the prior year noted

above.

CAPITAL RETURNS

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

Our commitment, in order of priority, is to:

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

Net debt² was \$1,104 million at year-end, a decrease of \$177 million from \$1,281 million at 31 December 2017. As part of our strategy to expand in higher growth markets, we expect to participate actively in value-enhancing M&A opportunities, and I am pleased with progress of our REGENETEN business, acquired from Rotation Medical in Q4 2017, which exceeded expectations throughout 2018. We have a strong balance sheet and substantial capacity for acquisitions. Appropriate financing for larger acquisitions would be considered on a case-by-case basis, as opportunities arise.

CETERIX ACQUISITION

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

EFFICIENCY

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

We are on track across all three workstreams of 1) Manufacturing, Warehousing and Distribution, 2) General and Administrative (G&A) Expenses, and 3) Commercial Effectiveness. APEX is expected to drive an annualised benefit of \$160 million by 2022 for a one-off cost of \$240 million.

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

Graham Baker

Chief Financial Officer

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

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

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

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

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

UK'S WITHDRAWAL FROM THE EU

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

OUTLOOK

Our 2019 guidance for further improvement in underlying performance at the top and bottom line is an important step in realising our medium-term ambition to outgrow our markets. In terms of revenue, we expect our underlying growth to be in the range of 2.5% to 3.5% in 2019. On a reported basis this equates to a range of around 1.8% to 2.8% at exchange rates prevailing on 1 February 2019 and including the effect of the Ceterix acquisition.

We expect 2019 trading profit margin to be in the range of 22.8% to 23.2%, a further 40 80bps improvement over 2018, excluding the one-off 50bps legal settlement benefit. The tax rate on trading results for 2019 is expected to be in the range 19% to 21%, subject to any material changes to tax law, or other one-off items.

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

Yours sincerely,

Graham Baker

Chief Financial Officer

Revenue		
\$4,904m		
Reported		Underlying ¹
+3%	+2%	
Earnings per share EPS		
76.0¢		13%
Adjusted earnings per share (EPSA)		
100.9¢		+7%

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

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

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Financial review

We have a strong balance sheet and substantial capacity for acquisitions

GROUP PERFORMANCE

	2018	2017	Change
	\$ million	\$ million	\$ million
Consolidated income statement			
Revenue	4,904	4,765	139
Operating profit	863	934	(71)
Trading profit ¹	1,123	1,048	75
Profit before tax	781	879	(98)
Attributable profit	663	767	(104)
EPS	76.0¢	87.8¢	(11.8¢)
EP ^{SA} ¹	100.9¢	94.5¢	6.4¢

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:

	Reported		Reconciling items			
	2018	2017	growth	Underlying growth	Acquisitions/ Disposals	Currency impact
	\$ million	\$ million	%	%	%	%
US	2,354	2,306	2%	1%	1%	0%
Other Established Markets ²	1,693	1,658	2%	0%	0%	2%
Emerging Markets ²	857	801	7%	8%	0%	(1%)
Total	4,904	4,765	3%	2%	0%	1%

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

	2018	2018%	2017	2017%
	\$ million		\$ million	
Operating profit	863	17.6%	934	19.6%

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Acquisition and disposal related items	(7)	(0.1%)	(10)	(0.2%)
Restructuring and rationalisation costs	120	2.4%	–	–
Amortisation and impairment of acquisition intangibles	113	2.3%	140	2.9%
Legal and other	34	0.7%	(16)	(0.3%)
Trading profit	1,123	22.9%	1,048	22.0%

DIVIDENDS

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

RETURN ON INVESTED CAPITAL

Return On Invested 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 decreased from 14.3% in 2017 to 12.5% in 2018 as a result of the reduction in operating profit.

ROIC is defined as:

Net Operating Profit less Adjusted Taxes
 (Opening Net Operating Assets +
 Closing Net Operating Assets)/2

BALANCE SHEET

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

Goodwill decreased by \$34 million primarily as a result of foreign currency movements. Intangible assets decreased by \$161 million with amortisation and impairment of \$179 million and foreign currency movements of \$14 million partially offset by net additions of \$32 million.

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

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

CASH FLOW STATEMENT

	2018	2017	Change
	\$ million	\$ million	\$ million
Consolidated cash flow statement			
Cash generated from operations	1,108	1,273	(165)
Trading cash flow ¹	951	940	11

Free cash flow ¹	584	714	(130)
-----------------------------	-----	-----	-------

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

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

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

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 debt³ decreased from \$1,281 million at the beginning of 2018 to \$1,104 million at the end of 2018, representing an overall decrease of \$177 million.

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

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

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

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

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

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

Risk Report

Our risk management process

Our approach to risk

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

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

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

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

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

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

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

BOARD OF DIRECTORS AND BOARD COMMITTEES

- Responsible for regular oversight of risk management and for our annual strategic risk review

- Monitors risks through Board processes (Strategy Review, Disclosures, M&A, Investments, Disposals) and Committees (Audit and Compliance & Culture), management reviews and 'deep dives' of selected risk areas
 - The Audit Committee is responsible for ensuring oversight of the process by which risks relating to the Company and its operations are managed and for reviewing the operating effectiveness of the Group's Risk Management process
-

EXECUTIVE COMMITTEE SITTING AS GROUP RISK COMMITTEE

Reviews external/internal environment for emerging risks

Reviews risk register updates from Business Area Risk Groups

Identifies significant risks and assesses effectiveness of mitigating actions

BUSINESS AREA

Business Area Risk Champions provide support to ensure a framework is designed and implemented for alignment to the requirements of the Enterprise Risk Management Framework

Carry out day-to-day risk management activities

Identify and assess risk

Implement strategy and mitigating actions to treat risk within Business Area

Business Area Risk Champions lead regular risk register updates

GROUP RISK TEAM

Manages implementation of all aspects of the Group's approach to Enterprise Risk Management including implementation of processes, tools and systems to identify, assess, measure, manage, monitor and report risks

Facilitates implementation and coordination through Business Area Risk Champions

Provides resources and training to support process

Regular risk reporting to the Executive Committee

Prepares Board and Group Risk Committee reports

ANNUAL ASSESSMENT OF EFFECTIVENESS – INTERNAL AUDIT AND CONTROL FUNCTIONS

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

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

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

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

2 Gross (inherent) risk assessment

ASSESSING the level of inherent (gross) risk.

3 Current control identification
IDENTIFYING existing controls to mitigate risks

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

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

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

7 Monitoring and review

MONITORING of
risks and actions by
management, the
accountable
Executive and
Board.

RISK REPORT continued

2018 principal risks

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

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

BUSINESS CONTINUITY AND BUSINESS CHANGE

Operating with a global remit, increased outsourcing, more sophisticated materials and the speed of technological change in an already complex manufacturing process leads to greater potential for disruptive events. Ensuring our ability to continually execute and operate key sites and facilities in order to develop, manufacture and sell our products within this environment is a key strategic imperative of the organisation. In addition, the pace and scope of our business ‘change’ initiatives increases the execution risk that benefits may not be fully realised, costs of these changes may increase, or that our business as usual activities may not perform in-line with our plans.

Examples of risks	Risk Tolerance
Failure or significant performance issues experienced at critical/single source facilities.	In operating our business, executing our change programmes and in
Disruption to manufacturing at single or sole source facility (lack of manufacturing redundancy).	managing our suppliers and facilities we have a low to moderate tolerance for this risk.
Supplier failure impacts ability to meet customer demand (single source suppliers).	Change from 2017 No change.
Natural disaster	

impacts
ability to
meet
customer
demand.

Significant
'change'
prevents our
projects and
programmes
such as
APEX
achieving
the intended
benefits and
disrupts
existing
business
activities.

Actions taken by management [Link to strategy](#)

Our Comprehensive Strategic
product quality processes and controls are in place from design to customer supply. [Imperative to 'Become the best owner' requires us to ensure we remain](#)

Emergency and incident management and business recovery plans are in place at major facilities and [sustainable into the future and through periods of business change.](#)

for key products and key suppliers. [Oversight Board](#)

Undertaking risk based review

programmes
for critical
suppliers.

Project
management
governance
and toolkits
and project
steering
committee
oversight to
support
successful
execution of
programme
and projects.

Executive
Committee
and Audit
Committee
oversight of
Risks to
change
programmes.

Brexit
Steering
Group
regularly
monitors the
evolving
impact of
Brexit and
oversees our
response.

CYBER SECURITY

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

Examples of risks	Risk Tolerance
Loss of intellectual property/major data privacy breach or significant impact on business operations from Malware or Ransomware outbreak.	In managing our cyber risk and the possible disruption and reputational impact we have a low to moderate tolerance for Cyber Security Risk. Change from 2017
Cyber security is not considered in the design of new products with more products being connectable/having embedded software. Actions taken by management	No change. Link to strategy
Security information and event management (SIEM) in place provides real-time analysis of security alerts generated by applications and network hardware.	Our Strategic Imperative to 'Transform the business through enabling technologies' requires us to deliver

Annual penetration testing and quarterly vulnerability testing. Endpoint protection and Intrusion detection/prevention technology solutions in compliance with laws and regulations and in a way that protects any vulnerability to Cyber Risk. Oversight

The adoption of additional authentication tools to reduce the likelihood of remote attacks. Audit Committee

Annual mandatory training and continuous awareness training for end-users.

Security governance structure in place including a Cyber Security Steering Committee.

Further strengthening governance including a programme to monitor cyber security capabilities and controls, technical and governance matters.

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

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

Examples of risks	Risk Tolerance
<p>Defects in design or manufacturing of products supplied to, and sold by, the Group could lead to product recalls or product removal or result in loss of life or major injury.</p>	<p>Our response to this risk continues to be critical and our ability to align the standards required to ensure safe and compliant products is the key driver for our</p>
<p>Significant non-compliance with policy, regulations or standards governing products and operations regarding registration, manufacturing, distribution, sales or marketing.</p>	<p>extremely low tolerance for risk in this area. Change from 2017</p> <p>No change.</p>
<p>Failure to obtain proper approvals for new or changed technologies, products or processes.</p>	
<p>CE certificates issued by UK notified bodies prior to the</p>	

withdrawal
date may be
rendered
void post
Brexit.

Actions
taken by
management

Link to
strategy

Comprehensive
and
documented
product
quality
processes
and controls
from design
to customer
distribution
are in place.

Our
Strategic
Imperative
to 'Become
the best
owner'
requires us
to operate
effectively
and
efficiently
and to
produce

Standardised
monitoring
and
compliance
with quality
management
practices
through our
Global
Quality
Assurance
and
Regulatory
Affairs
organisation.

compliant
products of
the highest
quality to
provide
safe and
effective
solutions to
our
customers.
Oversight

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

Board
Compliance &
Culture
Committee

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

Brexit
working
group is in
place
considering
various
deal/no deal
scenarios.

RISK REPORT continued

NEW PRODUCT INNOVATION, DESIGN & DEVELOPMENT INCLUDING INTELLECTUAL PROPERTY

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

Examples of risks

Failure to develop an appropriate pipeline of commercially successful products to meet and anticipate the needs of our customers ahead of the competition.

Insufficient long-term planning to respond to competitor disruptive entries into marketspace.

Inadequate innovation due to low Research & Development (R&D) investment, R&D skills gap or poor product development execution.

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

Competitors may assert patents or other intellectual property rights against the Company, or fail to respect the Company's intellectual property rights. Actions taken by management

Global R&D organisation and governance framework providing strategic direction for allocation of R&D investments across all businesses. Clear stage-gate process to continually evaluate R&D investments decisions and development of new products.

Enhanced relationship with Commercial team to focus on developing products that customers need.

Strengthened Clinical Affairs programme integrated with Global Marketing.

Risk Tolerance

In pursuit of our strategy to be innovative in our product offering we have a moderate to high tolerance for risk. Change from 2017

Reduced risk.

Link to strategy

Our Strategic Imperative to 'Transform the business through enabling technologies' depends heavily on our ability to continue to develop new innovative

<p>Cross functional New Product Design and R&D processes focused on identifying new products and potentially disruptive technologies and solutions.</p>	<p>products and bring them to market. Oversight</p>
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<p>Monitoring of external market trends and collation of customer insights to develop product strategies.</p>	<p>Board</p>
---	--------------

Careful attention to intellectual property considerations.

TALENT MANAGEMENT

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

Examples of risks

Loss of key talent, high attrition and lack of appropriate succession planning in context of required skillsets for future business needs.

Loss of competitive advantage due to an inability to attract and retain Top Talent.

Loss of intellectual capital due to poor retention of talent.

Actions taken by management

Talent planning and people development processes are well established across the Group. Talent and succession planning is discussed annually by the Board and regularly by the Executive Committee and Nomination & Governance Committee.

Identification of high performing individuals and practices to plan for the succession of key roles.

Consistent and robust performance management process.

Risk Tolerance

We have a moderate tolerance for this risk.

Change from 2017

No change.

Link to strategy

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

Development of strategic skills Oversight
resourcing plan by functional Board
areas.

PRICING AND REIMBURSEMENT

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

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

Examples of risks	Risk Tolerance
<p>Reduced reimbursement levels and increasing pricing pressures.</p> <p>Systemic challenge on number of elective procedures.</p> <p>Lack of compelling health economics data to support reimbursement requests.</p> <p>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.</p>	<p>In implementing innovative pricing strategies, we have a moderate to high tolerance for risk and are willing to accept certain risks in pursuit of new business opportunities. Change from 2017</p>
<p>Actions taken by management</p> <p>Development of innovative economic product and service solutions for both Established and Emerging Markets.</p> <p>Appropriate breadth of portfolio and geographic spread to mitigate exposure to localised risks.</p> <p>Incorporating health economic components into the design and development of new products.</p> <p>Emphasising value propositions tailored to specific stakeholders and geographies through strategic investment and</p>	<p>No change. Link to strategy</p> <p>Our Strategic Imperative to 'Achieve the full potential of our portfolio' depends on our ability to sell our products profitably in spite of increased pricing pressures from payers. Oversight</p>

marketing programmes.

Board

MERGERS AND ACQUISITIONS

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

Examples of risks

Failure to identify appropriate acquisitions or to conduct effective acquisition due diligence.

Failure to integrate newly acquired businesses effectively, including integration with Company standards, policies and financial controls.

Risk

Tolerance

In acquiring new businesses and business models, we have a moderate to high tolerance for commercial risk and are willing to accept certain risks in pursuit of new business. Change from 2017

No change. Link to strategy

Actions taken by management

Acquisition activity is aligned with corporate strategy and prioritised towards products, franchises and markets identified to have the greatest long-term potential.

Clearly defined investment appraisal process based on return on capital, in accordance with Capital Allocation Framework and comprehensive post-acquisition review programme.

Our Strategic Imperatives to 'Expand in high-growth segments' and 'Transform the business through enabling technologies' depend on our ability to identify the right acquisitions, to conduct

Undertaking detailed and thorough due
comprehensive diligence
cross-functional due and to
diligence prior to integrate
acquisitions. acquisitions
effectively.

Compliance risks included Oversight
as part of due diligence
reviews, integration plans Board
and reporting for
acquisitions.

RISK REPORT continued

LEGAL AND COMPLIANCE RISKS

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

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

Examples of risks

Failure to act in an ethical manner consistent with our Code of Conduct.

Violation of anti-corruption or healthcare laws, breach by employee or third party representative.

Misuse or loss of personal information of patients, employees, research subjects, consumers or customers results in violations of data privacy laws, including General Data Protection Regulations.

Actions taken by management

Ethics & Compliance Committee oversees our ethical and compliance practices.

Global compliance programme, policies and procedures.

All employees are required to undertake annual training and to certify compliance on an annual basis with our Code of Conduct and Business Principles.

Group monitoring and auditing programmes in place.

Confidential independent reporting channels for employees and third parties to report concerns.

Risk Tolerance

In complying with legal and compliance requirements, we have an extremely low tolerance. Change from 2017

No change.

Link to strategy

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

Board Compliance & Culture Committee

COMMERCIAL EXECUTION

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

Examples of risks	Risk Tolerance
<p>Failure to execute our strategy adequately from high level ambition to specific actions to make the ambition a reality.</p>	<p>We have a low to moderate tolerance level for commercial execution risk. Change from 2017</p>
<p>Inability to keep pace with significant product innovation and technical advances to develop commercially viable products.</p>	<p>No change.</p>
<p>Failure to adapt our priorities and execution appropriately when conditions change meaning that transformational programmes do not deliver the expected outcomes.</p>	
<p>Failure to engage effectively with our key stakeholders to meet their evolving needs leading to loss of customers.</p>	
<p>Actions taken by management</p>	<p>Link to strategy</p>
<p>Global R&D organisation and supporting governance framework.</p>	<p>Our Strategic Imperatives to 'Achieve the full potential of our portfolio', 'Transform the business through enabling technologies' and 'Expand in high-growth segments'</p>
<p>Improved market development and launch execution – commitment to win profitably in our target markets.</p>	
<p>Strategic planning process clearly linked to business and Group Risk.</p>	
<p>Global transformational programmes in place providing agile opportunities</p>	

for efficiencies, growth and a strengthened competitive position.

requires excellent commercial execution. Oversight

Board

POLITICAL AND ECONOMIC

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

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

Examples of risks

Macro-economic uncertainty or downturn in the UK economy as a result of Brexit.

Regulatory risk whereby certificates issued by UK Notified Bodies are no longer recognised in EU following March 2019.

Global political uncertainty – regarding trade policy.

Implementation of healthcare reforms and/or protectionist measures and regulation or legislation in local markets.

Exchange rate volatility.

The availability of markets and market access rights.

Impact on strategy and operations.

Increases in import and labour costs.

Retention of skilled labour and recruitment concerns.

Increases in tariffs and restrictions on global trade.

Actions taken by management

Continued engagement with governments, administrations and regulatory bodies.

The Group has a Brexit committee which meets regularly and is split

Risk Tolerance

In preparing for Brexit and managing risk arising from changes to our political economical environment, we have a low to moderate tolerance. Change from 2017

New risk previously incorporated into Business Change.

Link to strategy

Our Strategic Imperative to ‘Become the best owner’ requires us to operate

into a number different work streams namely:

Regulatory – the most complex work stream considering product registration.

Supply chain – considering the impacts on import and export requirements in UK and Europe; supply routes, managing inventory levels in the UK and Europe to minimise disruption from border clearance and managing labelling changes required as a result of the regulatory changes.

UK and Ireland ('UKI') market – considering issues expected to impact the UKI specifically the Irish border issue – including whether a changed route to market is required in Ireland.

HR – considering issues such as impact on EU workers currently employed in UK and future mobility considerations.

Finance – considering issues such as impact on tax including EU trading arrangements and the VAT implications of the changes and the impact on financial reporting, eg EU/UK endorsement of IFRS.

Improved engagement and monitoring/lobbying on localisation initiatives.

effectively within different global political situations, which change constantly.
Oversight

Board

RISK REPORT continued

‘Deep Dives’ and reviews completed in the year

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

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

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

BOARD AND AUDIT COMMITTEE ‘DEEP DIVES’ AND REVIEWS

LEGAL, COMPLIANCE AND QUALITY

During the year, the Ethics & Compliance Committee considered papers from the quality and regulatory and legal and compliance functions covering topics such as preparations for EU Medical Device Regulations, FDA & Notified Body inspections, outcomes of internal investigations, reviews of legal issues and a review of sexual harassment policies and claims.

RESEARCH AND DEVELOPMENT FUNCTIONAL OVERSIGHT

During the year, the Board received a report from the R&D function which included a focus on the risks associated with the R&D programme and strategies to manage these risks.

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

MANUFACTURING OPERATIONS

HR

M&A

During the year, the Board has received a number of presentations from the global operations team considering the risks in particular associated with the manufacturing footprint and the supply chain and proposals to mitigate these risks.

The Board has reviewed and approved all Executive Officer changes during the year within the context of the overall strategy and have been kept updated on management actions to implement the new culture pillars.

Each Board meeting considers Corporate Development within the context of the Group Strategy and also reviews specific acquisitions. During the year, the Board also undertook retrospective reviews of previous acquisitions compared to expectations in the original deal models.

IT/CYBER

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

GROUP RISK TEAM 'DEEP DIVES'

A series of planned 'Deep Dives' have been completed in the year across our Business Risk Areas, including Global Manufacturing, Strategic Sourcing, Supply Chain, Global Quality and Regulatory, Global Business Services and IT. These reviews were introduced in 2017 to supplement reports provided to the Board and primarily cover an 'independent' assessment of compliance to the expected Risk Management Framework and in particular the adequacy of stated mitigating activities. The results are reported through the Risk Champions and Accountable Executives to the Audit Committee and are tracked and monitored to resolution by the Group Risk Team.

2019 Risk Management Plan

Our work will continue to evolve in 2019 and we will strengthen our approach to managing risks across the organisation, including our business areas and product groups.

We will continue to ensure a truly collaborative approach to risk management with risk accountability sitting squarely with management and a proactive Group Risk function influencing decision making through effective challenge and timely consultation.

2019 RISK MANAGEMENT TIMELINE

Q1 2019	Q2 2019	Q3 2019	Q4 2019	Q1 2020
INTERNAL AUDIT				
Risk Management Effectiveness Review report to Audit Committee			2020 Risk Based Internal Audit Plan Preparation	Risk Management Effectiveness Review report to Audit Committee
GROUP RISK TEAM				
Refresh Enterprise Risk Management Policy and Manual	Risk training Report to Audit Committee Facilitate 'top down' review process		Prepare 2020 Enterprise Risk Management Strategy Prepare Review of Principal Risks Report to Audit Committee	Refresh Enterprise Risk Management Policy and process
BUSINESS RISK AREAS				
Quarterly Risk Review by leadership teams	Quarterly Risk Review by leadership teams Review Principal Risks and map to Strategic Imperatives	Quarterly Risk Review by leadership teams Risk Register refresh and submission to Group Risk Team annual certification	Quarterly Risk Review by leadership teams	Quarterly Risk Review by leadership teams

EXECUTIVE COMMITTEE

Review reports from Group Risk Team	Review reports from Group Risk Team	'Top Down' review of Principal Risks	Approve Principal Risks	Review reports from Group Risk Team
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AUDIT COMMITTEE

Review and approval of the Group's 2018 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	Review and approval of the Group's 2019 Risk Management Process and Viability Statement
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BOARD

Approve Principal Risks	Review of Principal Risks	Approve Principal Risks
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RISK REPORT continued

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 41–49 of this Annual Report.

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

- The Audit Committee reviewed the Risk Management process at their meetings in February, July, September and December, receiving presentations from the Group Risk function, explaining the processes followed by management in identifying and managing risk throughout the business.
- In October, a series of detailed one-to-one discussions were held with each member of the Executive Committee and the Group Risk Team. In these discussions, the Executives were asked to consider the significant risks which they believed could seriously impact the profitability and future prospects of the Company and the principal risks that would threaten its business model, future performance, solvency or liquidity.
- As part of the strategy business updates in September, the Board considered and discussed the Principal Risks which could impact the business model over the next three years and discussed with the management team how these risks were being managed and mitigated.
- Throughout the year, a number of ‘deep dives’ and reviews into different risks were conducted by the Board, the Audit Committee and the Ethics & Compliance Committee looking into the nature of the risks and how they were mitigated, as detailed on page 48 of this Annual Report.
- Throughout the year, a number of ‘deep dives’ into specific risk areas were conducted by the Group Risk Team, the results of which were presented to and discussed by the Audit Committee and are detailed on page 48 of this Annual Report.

ASSESSMENT PERIOD

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

SCENARIO TESTING

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

- In carrying out scenario modelling of the principal and significant risks on the following page we have also evaluated the impact of a severe but plausible combination of these risks actually occurring over the three-year period. We have considered and discussed a report setting out the terms of our current financing arrangements and potential capacity for additional financing should this be required in the event of one of the scenarios modelled occurring.
 - We are satisfied that we have robust mitigating actions in place as detailed on pages 42–47 of this Annual Report. We recognise, however, that the long-term viability of the Company could also be impacted by other, as yet unforeseen, risks or that the mitigating actions we have put in place could turn out to be less effective than intended.
-

2018 SCENARIOS MODELLED

SCENARIO 1 – PRICING AND REIMBURSEMENT PRESSURES

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

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

[Link to strategy](#)

[Link to Principal Risks](#)

- Achieve the full potential of our portfolio
- Pricing and Reimbursement

SCENARIO 2 – OPERATIONAL RISK

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

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

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

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

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

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

[Link to strategy](#)

[Link to Principal Risks](#)

- Become the best owner
- New Product Innovation, Design & Development Including Intellectual Property
- Transform the business through enabling technologies
- Commercial Execution
- Achieve the full potential of our portfolio
- Business Continuity and Business Change

SCENARIO 3 – LEGAL REGULATORY AND COMPLIANCE RISKS

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

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

Bribery and corruption claims – giving rise to significant fines.

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

[Link to strategy](#)

[Link to Principal Risks](#)

- Become the best owner
- Legal and Compliance
- Quality and Regulatory

SCENARIO 4 – CYBER SECURITY

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

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

[Link to strategy](#)

[Link to Principal Risks](#)

- Transform the business through enabling technologies
- Cyber Security

OTHER

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

[Link to strategy](#)

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

[Link to Principal Risks](#)

– Become the best owner

– Political and Economic

VIABILITY STATEMENT

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

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

By order of the Board, on 21 February 2019.

Susan Swabey

Company Secretary

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Governance	
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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 Compliance & Culture 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

www.frc.org.uk/getattachment/ca7e94c4_b9a9_49e2_a824_ad76a322873c/UK-Corporate-Governance-Code-April_2016.pdf

In addition, we are making progress in complying with certain aspects of the 2018 Corporate Governance Code early.

The Directors' Report comprises pages 2, 10, 11, 24, 25, 32, 39, 40, 83, 116, 154, 156, 173, 187, 209 of the Annual Report.

Chair's introduction

We are making progress implementing the 2018 UK Corporate Governance Code.

DEAR SHAREHOLDER,

I am pleased to present the governance section of our Annual Report, which includes details about the Board and an explanation of our individual roles and responsibilities. We also summarise the activities of the Board during the year and the Chair of each Board Committee discusses the activities of that Committee during the past year.

The publication by the Financial Reporting Council in 2018 of the new UK Corporate Governance Code (the 'Code') and the Guidance on Board Effectiveness has caused us to reconsider some aspects of how we will operate as a Board going forward. We are in the process of reorganising the composition and the responsibilities of some of the Board Committees to reflect the new emphasis in the Code on listening to the employee voice and having regard to the views of all our key stakeholders. We explain our intended approach in the reports from the Nomination & Governance Committee and the Ethics & Compliance Committee, which will become the expanded Compliance & Culture Committee. The scope of the Remuneration Committee has also been broadened and this is discussed in the Remuneration Report. These changes are reflected in revised terms of reference, which are available on our website and in revised Committee memberships, explained further in the individual Committee reports.

We have also included a section explaining how the Board has fulfilled its duties towards our key stakeholders – our employees, our customers and suppliers, our investors and governments and regulators – in 2018, and how we plan to build on this in 2019.

In particular, we have considered how we can listen better to the employee voice. We feel that as a unitary Board, this is very much the responsibility of the Board as a whole and that this responsibility should not fall to any one designated director or to an employee representative. We are a global company operating out of multiple locations, with employees coming from many different perspectives. Elsewhere in this report, you will have read about the work Namal and the executive team have done in the past year, developing the new purpose, strategic imperatives and culture pillars. This work included engagement with a large number of our employees across the world at all levels of the organisation. The Board intends to build on these now established means of engagement, so that we too can listen effectively and respond to the employee voice. This programme will be developed for us by the expanded Compliance & Culture Committee and will be in addition to the engagement we currently have with employees when we undertake site visits as part of our Board programme.

CHANGES TO THE BOARD IN 2018

During the year to 31 December 2018, there were the following changes to the Board:

1. Namal Nawana joined the Board as Chief Executive Officer on 7 May 2018.
2. Olivier Bohuon retired from the Board as Chief Executive Officer on 7 May 2018.

3. Roland Diggelmann joined the Board as a Non-Executive Director and Member of the Audit Committee on 1 March 2018.
4. Joseph Papa retired from the Board on 12 April 2018.

At the Annual General Meeting to be held on 11 April 2019 there will be some additional Board changes. Ian Barlow, our Senior Independent Director and former Chair of the Audit Committee will be retiring after nine years' service to the Company. Michael Friedman, Chair of our Compliance & Culture Committee will also be retiring after six years' service.

We would like to thank both Ian and Michael for their outstanding contribution to the Company through periods of change. Michael has given us deeper insight into regulatory matters and Ian has been a valuable support to me on many matters, most recently in finding Namal Nawana, our new Chief Executive Officer.

Robin Freestone will succeed Ian as Senior Independent Director and Marc Owen will succeed Michael as Chair of the expanded Compliance & Culture Committee. Over the course of the coming months, we shall be undertaking a search for a new Non-Executive Director with recent and relevant financial experience to be our financial expert and in time take over from Robin as Chair of the Audit Committee.

Roberto Quarta

Chair

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Leadership

Our Board of Directors

ROBERTO QUARTA (69)	NAMAL NAWANA (48)	GRAHAM BAKER (50)
Chair	Chief Executive Officer	Chief Financial Officer
<p>Joined the Board in December 2013 and appointed Chair following election by shareholders at the 2014 Annual General Meeting. He was also appointed Chair of the Nomination & Governance Committee and a Member of the Remuneration Committee on that day.</p>	<p>Joined the Board and was appointed Chief Executive Officer on 7 May 2018. He will stand for election by shareholders at the AGM on 11 April 2019. He is based in Andover, US.</p>	<p>Joined the Board as Chief Financial Officer in March 2017. He is based in London, UK.</p>
Career and experience	Career and experience	Career and experience
<p>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 Chair, until 2007.</p>	<p>Prior to Smith & Nephew Namal was Chief Executive Officer and a member of the Board of Medical Diagnostics Company Alere Inc, until its \$8 billion acquisition by Abbott in 2017. Before joining Alere, Namal spent more than 15 years at Johnson & Johnson in progressively senior leadership roles globally including the role of Worldwide President of Johnson & Johnson's multi-billion dollar spine franchise, DePuy Synthes Spine. In addition to his role as CEO of Smith & Nephew, Namal is also a member of the Board of Directors of Hologic, Inc. a Nasdaq listed company and Advamed (Advanced Medical Technology Association).</p>	<p>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.</p>
<p>He has held several board positions, including Non-Executive Director of Powergen plc, Equant N.V., BAE Systems plc and Foster Wheeler AG.</p>	<p>Namal holds an undergraduate degree in Mechanical Engineering and a Masters degree in Medical Science from the University of Adelaide, South Australia, as well as an MBA from Henley Management</p>	<p>Most recently, Graham was Chief Financial Officer of generic pharmaceuticals company Alvogen.</p>
	Skills and competencies	Skills and competencies

His previous Chairmanships include Italtel SpA, Rexel S.A., IMI plc and SPIE SA. He is currently Chair 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.

College. He is a global leader with broad experience in healthcare and medical technology.

Nationality

Australian/French

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 Chair 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 in 2018. Roberto also conducted the search resulting in the appointment of Namal Nawana as our CEO in 2018.

Nationality

American/Italian

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 (63)	THE RT. HON BARONESS	ROLAND DIGGELMANN (51)
Independent Non-Executive Director	VIRGINIA BOTTOMLEY OF	Independent Non-Executive
	NETTLESTONE DL (70)	Director
Appointed Independent Non-Executive	Independent Non-Executive Director	Appointed Independent
Director in December 2014 and Member of	Appointed Independent Non-Executive	Non-Executive Director and
the Remuneration Committee and	Director in April 2012 and Member of	Member of the Audit Committee
Compliance & Culture Committee.	the Remuneration Committee and	on 1 March 2018. He was elected
Career and experience	Nomination & Governance Committee	by shareholders at the AGM on
	in April 2014 and will join the	12 April 2018. He will join the
Vinita holds an MBA from the Jamnalal	Compliance & Culture Committee in	Compliance & Culture
Bajaj Institute of Management Studies,	April 2019.	Committee in April 2019.
University of Bombay and a BA in	Career and experience	Career and experience
Economics from the University of Delhi. She	Virginia gained her MSc in Social	Roland studied Business
commenced her career in India with a Tata	Administration from the London	Administration at the University
Group Company, and then joined Cadbury	School of Economics following her	of Berne. In 1995, he joined
India, subsequently working with Cadbury	first degree. She was appointed a Life	Sulzer AG as Manager Strategic
Schweppes plc in the UK, Nigeria and South	Peer in 2005 following her career as a	Planning and progressed into
Africa. She has held a number of senior	Member of Parliament between 1984	further senior roles over the years
global positions in marketing and general	and 2005. She served successively as	until his appointment as
management at The Coca-Cola Company	Secretary of State for Health and then	Executive Vice President, Sales
based in the US and South America,	Culture, Media and Sport. Virginia	Europe and Asia Pacific from
becoming President of the Andean Division	was formerly a Director of Bupa and	2002 to 2004 for Sulzer Medica
in 1999 and VP, Corporate Strategy in 2001.	AkzoNobel NV. She is currently a	(later known as Centerpulse).
In 2003, she joined Zyman Group, LLC, a	Director of International Resources	Roland joined Zimmer Group in
US-based consultancy, as Managing	Group Limited, where she is Chair of	2004, in the role of Managing
Principal. Vinita was MD and CEO of	Board & CEO Practice at Odgers	Director of Zimmer Japan and
Britannia Industries Limited, a leading Indian	Berndtson. She is a member of the	then later in 2006 as Senior Vice
publicly listed food company from 2005 to	International Advisory Council of	President, EMEA until 2008.
2014. Currently, Vinita is NED of Syngene	Chugai Pharmaceutical Co.,	Roland joined Roche Diagnostics
International Limited, Bunge Limited and	Chancellor of University of Hull and	in 2008 starting as president of
CRISIL India (a Standard & Poor Company).	Sheriff of Kingston upon Hull. She is a	Asia Pacific before assuming the
She is also a member of the Advisory Board	Trustee of The Economist Newspaper.	role of Chief Executive Officer
of PwC India.	Skills and competencies	of the Diagnostics Division of F.
Skills and competencies	Virginia's extensive experience within	Hoffmann-La Roche Ltd from
Vinita has an impressive track record of	Government, particularly as Secretary	2012 until September 2018.
achievement with blue-chip global	of State for Health, brings a unique	Skills and competencies
corporations in multiple geographies		
including India, Africa, South America, US		

and UK, all key markets for Smith & Nephew. Her strong appreciation of customer service and marketing brings deep insight as Smith & Nephew continues to develop innovative ways to serve our markets and grow our business.

Nationality

Indian

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.

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 is of great value to Smith & Nephew.

Nationality

Swiss

Nationality

British

Leadership

Our Board of Directors continued

ERIK ENGSTROM (55)	ROBIN FREESTONE (60)	MARC OWEN (59)
Independent Non-Executive Director	Independent Non-Executive Director	Independent Non-Executive Director
Appointed Independent Non-Executive Director in January 2015 and Member of the Audit Committee. He will join the Nomination & Governance Committee in April 2019.	Appointed Independent Non-Executive Director and Member of the Audit Committee and the Remuneration Committee in September 2015 and Chair of the Audit Committee in April 2017. Robin will succeed Ian Barlow as Senior Independent Director following the AGM on 11 April 2019 and join the Nomination & Governance Committee.	Appointed Independent Non-Executive Director and Member of the Audit Committee in October 2017 and Member of the Compliance & Culture Committee in March 2018. He will be appointed chair of the Compliance & Culture Committee in April 2019.
Career and experience	Career and experience	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	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, Chair of the 100 Group and Senior Independent Director and Chair of the Audit Committee of Cable & Wireless Communications plc. Robin is NED and Chair of the Audit Committee at Capri Holdings Ltd, (formerly Michael Kors Holdings Ltd). Robin became Chair of the ICAEW Corporate Governance Committee in 2017 and is currently a NED and Chair of the Audit Committee at MoneySupermarket.com plc. Robin will be	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

firm. Between 2004 and 2009, he was CEO of Elsevier, the division 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 and Nomination & Governance Committees.

Nationality

Swedish

appointed as Chair of their Board with effect from the conclusion of its Annual General Meeting on 9 May 2019.

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 is of value to Smith & Nephew as it continues to grow globally and in different markets. He brings financial expertise and insight as Chair 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

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 role came in 2014 where he was appointed Chair 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 and makes him ideally placed to Chair the Compliance & Culture Committee.

Nationality

British

DIRECTORS WHO SERVED
DURING 2018 RETIRING AT
ANNUAL GENERAL MEETING

ANGIE RISLEY (60)

Independent Non-Executive Director

Appointed Independent Non-Executive Director in September 2017 and appointed Chair of the Remuneration Committee on 12 April 2018.

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 HRD 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 and Serco Group plc, and now Smith & Nephew. At Serco she was the Chair of the Remuneration Committee. Previously she has attended Remuneration Committees of Whitbread, Lloyds Banking Group, Arriva and attends Sainsbury's today. She is also a Non-Executive Director on the Sainsbury's Bank Board.

Skills and competencies

Angie is a well-regarded FTSE 100 Human Resources Director, proven Non-Executive

IAN BARLOW (67)

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 Compliance & Culture Committee in October 2014 and Senior Independent Director and Member of the Nomination & Governance Committee on 6 April 2017. Ian will retire from the Board at the Annual General Meeting on 11 April 2019 and will not stand for re-election.

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.

MICHAEL FRIEDMAN (75)

Independent Non-Executive Director

Appointed Independent Non-Executive Director in April 2013 and Chairman of the Compliance & Culture Committee in

SUSAN SWABEY (57)

Company Secretary

Joined Smith & Nephew in May 2009 as Company Secretary with responsibility for Board support and corporate governance, employee and executive share plans and subsidiary governance. In 2016, she also assumed responsibility for leading the group's risk management programme. She is based in Watford.

Career 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, remuneration, corporate transactions, group risk management, share registration, listing obligations, corporate social responsibility, pensions, insurance and employee and executive share plans.

Director and Remuneration Committee Chair. 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 an additional resource and sounding board for Smith & Nephew's own internal Human Resources function.

Nationality

British

August 2014. Michael will be retiring from the Board at the Annual General Meeting on 11 April 2019 and will not stand for re-election.

Career and experience

Michael is medically trained, specialising in Internal Medicine and Medical Oncology. He was formerly CEO of City of Hope in California, and also served as Director of the institution's cancer centre. 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 Administration (FDA). He has served on a number of boards in a non-executive capacity and is currently a NED of Celgene Corporation, MannKind Corporation and Intuitive Surgical, Inc.

Susan holds an MA from Corpus Christi College Oxford in Literae Humaniores and is a Fellow of the Institution of Chartered Secretaries: The Governance Institute. She is also Chair of ShareGift, the share donation charity, a member of the Financial Reporting Council Lab Steering Group and a frequent speaker on corporate governance and related matters.

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Leadership

Executive team

Namal Nawana is supported in the day-to-day management of the Group by Graham Baker, Chief Financial Officer, and a strong team of Executive Officers.

RODRIGO BIANCHI (58)

Interim President, Asia Pacific

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 now President of Asia Pacific. 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

BRAD CANNON (50)

President, Sports Medicine & ENT

Joined Smith & Nephew in 2012 and has since been the President of Smith & Nephew's Europe and Canada business, the Company's Chief Marketing Officer, and now serves as the President of the Global Sports Medicine and Ear, Nose and Throat business. He is based in Andover, US.

Skills and experience

Brad was most recently the Chief Marketing Officer and prior to that the President of Europe and Canada, where he successfully led the commercial business in those regions. He has also served as the 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

Italian

NEW COMMERCIAL MODEL: CREATION OF GLOBAL FRANCHISES

MASSIMILIANO COLELLA (50)	PHIL COWDY (51)	SIMON FRASER (51)
President, Europe, Middle East and Africa	Executive Vice President, Business Development & Corporate Affairs	President of Advanced Wound Management
Joined Smith & Nephew in 2013 as Senior Vice President for Mid-Tier Business based in Dubai, Massimiliano (Max to his colleagues and friends), afterwards took over the role of SVP Smith & Nephew AsiaPac in Singapore. Promoted to President Europe and Canada, he moved back to Europe in 2017. He is now President of Europe, Middle East and Africa. Massimiliano is based in Baar, Switzerland.	Joined Smith & Nephew in 2008 as Director of Investor Relations. From 2010 his responsibility expanded as Head of Corporate Affairs, including media, investor relations, global brand and government affairs, together with Strategic Planning. Between 2015 and 2018 he was also responsible for IT. In 2018 he took on additional responsibility for Business Development. He is based in London, UK.	Joined Smith & Nephew in January 2019 with commercial leadership responsibility for Advanced Wound Management in the US and global upstream marketing for the Advanced Wound Management Franchise. As part of his executive responsibilities Simon will also provide leadership for Healthcare Systems. Simon is based in Fort Worth, US.
Skills and experience	Skills and experience	Skills and Experience
Over his 26 years spent in the medical device industry, Massimiliano has held a number of national and international roles in Europe, Middle East and Asia. Before joining Smith & Nephew, Max worked for 21 years in Johnson & Johnson, leading a number of different businesses in Ethicon and DePuy Synthes franchises.	Prior to joining Smith & Nephew, Phil served as a senior Director at Deutsche Bank for 13 years, providing corporate finance and equity capital markets advice to a variety of UK based companies. He qualified as a chartered accountant with EY.	Simon brings to this role more than 25 years of experience across medical devices, pharmaceuticals and diagnostics, including wound management. Importantly, he is a purpose-driven and accomplished business leader who has successfully managed large, global commercial organisations with full P&L responsibility while growing business and earning market share.
Nationality	Nationality	Nationality
Italian	British	Prior to joining Smith & Nephew Simon was Group Vice President of Dentsply-Sirona's Dental Implant Global Business Unit. Prior to this Simon was Vice President, US Commercial Infectious Diseases including corporate accounts at Abbott Laboratories. Simon joined Abbott following the acquisition of Alere where he had three successful years as the President of Latin America. Prior to these roles, Simon had a 15 year career with Johnson & Johnson, where he held increasingly senior commercial roles spanning surgical devices, wound management, implants and pharmaceuticals including both global strategic marketing and P&L responsibilities.
Nationality	Nationality	Nationality

Leadership

Executive team continued

<p>MARK GLADWELL (43)</p>	<p>MELISSA GUERDAN (44)</p>	<p>SKIP KIIL (44)</p>
<p>President of Global Operations</p>	<p>Chief Quality and Regulatory Affairs Officer</p>	<p>President of Orthopaedics</p>
<p>Joined Smith & Nephew in August 2018 with responsibility for Global Manufacturing, Global Supply Chain, Global Procurement, Global Engineering and Global Operational Excellence, and all Operational Strategy and programmes including APEX projects related to Global Operations. Mark is based in Watford, UK.</p>	<p>Joined Smith & Nephew in July 2018 with responsibility for Quality and Regulatory Affairs and is based in Andover, US.</p>	<p>Joined Smith & Nephew in November 2018 with global responsibility for the Orthopaedics franchise, which includes Reconstruction, Trauma, Extremities and Robotics. Skip is based in Memphis, US.</p>
<p>Skills and experience</p>	<p>Skills and Experience</p>	<p>Skills and Experience</p>
<p>Mark joined Smith & Nephew from QIAGEN, a provider of sample and assay technologies for molecular diagnostics, applied testing, academic and pharmaceutical research. There he was Senior Vice President of Global Operations responsible for global manufacturing, supply chain, quality assurance and control, regulatory affairs, and global customer service.</p>	<p>Melissa brings more than 20 years of leadership experience in Quality and Regulatory Affairs spanning the pharmaceutical, medical device and biologics industries. Melissa has deep compliance and operations knowledge and has progressed through senior leadership roles in global organisations including Pfizer, Baxter, Covidien and Alere. Most recently, Melissa was Senior Vice President, Quality and Regulatory for Alere where she had executive responsibility for establishing enterprise vision, strategy and direction for all aspects of quality, compliance and regulatory affairs. Melissa is adept at inspiring diverse global organisations to achieve common goals and has consistently delivered material value at the enterprise level through transformational quality and regulatory improvement programmes.</p>	<p>Skip is a seasoned leader who brings a wealth of global experience from diverse medical technology companies, and importantly, significant global experience in Orthopaedics markets over an extended period. Prior to joining Smith & Nephew, Skip was most recently responsible for all Global Commercial Operations at NuVasive and member of the senior executive leadership team. Prior to this, Skip spent three years with Alcon, a division of Novartis Corporation, based in Geneva Switzerland where he served as Surgical Head, Europe, Middle East, Africa and Russia. While at Alcon, Skip led the successful commercial transformation of its \$1.1bn surgical business across both developed and emerging growth markets.</p>
<p>Mark is a seasoned operational leader bringing more than</p>	<p>Melissa holds a BA degree in Biology and Psychology, and holds an MBA from</p>	<p>Before joining Alcon, Skip had a successful 12 year career with Stryker Corporation, beginning in sales and holding progressively senior positions in commercial leadership in the US as well as</p>

20 years of experience in progressively senior operations roles across global organisations including DuPont, AGFA Medical Imaging, Johnson & Johnson, and Alere Inc. Mark has experience of working and living in Europe and the US and operating global manufacturing and supply chain organisations with a significant focus and track record in delivering operational excellence transformation programmes.

DePaul University.

Nationality

American

in global marketing. Skip also had general management experience in Japan, as well as group leadership responsibilities in Europe where he held the role of Vice President and General Manager of its Medical Surgical Group.

Nationality

American

Nationality

British

ELGA LOHLER (51)	CATHY O'ROURKE (46)	VASANT PADMANABHAN (52)
Chief Human Resources Officer	Chief Legal and Compliance Officer	President of Research & Development
<p>Joined Smith & Nephew in January 2002 as Director of HR and has since held progressively senior positions in Wound Management, Operations, Corporate Functions and Group. Elga became Chief Human Resources Officer in December 2015 and leads the Global Human Resources, Internal Communication and Sustainability Functions. Elga is based in Fort Worth, US.</p>	<p>Cathy joined Smith & Nephew in February 2013 and became Chief Legal Officer in May 2017 and Chief Legal and Compliance Officer in July 2018. Cathy heads up the Global Legal and Compliance functions and is based in Andover, US.</p>	<p>Vasant 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.</p>
Skills and Experience	Skills and Experience	Skills and Experience
<p>Elga has more than 25 years' Human Resources experience. Prior to joining Smith & Nephew, Elga held Human Resources roles at Transnet, Sensormatic (now Tyco) and Advanced Tissue Sciences, which was acquired by Smith & Nephew in 2002. Through these roles, Elga has developed deep expertise in strategy planning and development, organisational design and effectiveness, restructuring and integration and transformational change in support of business objectives. In her current roles, Elga is responsible for driving Smith & Nephew's human capital strategy across the enterprise in support of the company's overall business plan and strategic direction.</p>	<p>Prior to being appointed Chief Legal Officer, Cathy had various responsibilities within Legal as Assistant General Counsel – Litigation and Investigations. 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.</p>	<p>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, Programme 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.</p>
<p>Elga holds an undergraduate degree in Psychology and a Master's degree in Organizational Psychology, both</p>	<p>Nationality American</p>	<p>Nationality American</p>

from the University of Witwatersrand
in South Africa.

Nationality

American/South African

Leadership

Roles and composition

Whilst we all share collective responsibility for the activities of the Board, some of our roles have been defined in greater detail below.

CHAIR

- 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 effective two-way communication and debate with shareholders and stakeholders.
- Promoting high standards of corporate governance.
- Maintaining appropriate balance between stakeholders.

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

Maintaining relationships with shareholders.

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.

CHIEF EXECUTIVE OFFICER

- Developing and implementing Group strategy.
- Recommending the annual budget and three-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 Chair 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.

SENIOR INDEPENDENT DIRECTOR

- Chairing meetings in the absence of the Chair.
- Acting as a sounding board for the Chair 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 Chair, if necessary.

COMPANY SECRETARY

- Advising the Board on matters of corporate governance.
 - Supporting the Chair 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:

BOARD

Audit Committee	Remuneration Committee	Nomination & Governance Committee	Compliance & Culture Committee	Ad hoc committees
Provides independent assessments of the financial affairs of the Company and reviews financial statements and controls oversight of the risk management process and key risks, such as cyber security. Manages use	Determines remuneration policy and packages for the Executive Directors and Officers, having regard to the Group.	Reviews size and composition of the Board, succession planning, diversity and governance matters.	Reviews and monitors ethics and compliance, quality and regulatory matters across the Group.	Ad hoc committees may be established to review and approve specific matters or projects.
			Role to be expanded in 2019 to include oversight of culture, sustainability and stakeholder relationships.	

of
internal
and
external
auditors.

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The Board delegates the day-to-day running of the business to Namal Nawana, Chief Executive Officer, who is assisted in his role by the Executive Committee comprising the Executive team shown on pages 58 - 61. The governance framework below outlines the Executive Committee arrangements as follows:

EXECUTIVE COMMITTEE

The Executive Committee meets regularly and makes decisions collectively. It recommends and implements strategy, recommends budget and three-year plan to the Board for approval, ensures liaison between commercial and corporate functions, receives regular reports from sub-committees, reviews major investments, divestment and capital expenditure proposals and approves business development projects.

Monthly Operating Review	Franchise, Functional and Regional Leadership Meetings	Portfolio Innovation Board	Group Ethics & Compliance Committee
Wider group of senior commercial and financial leaders reviews monthly commercial and marketing and operating results against budget, identifying gaps and agreeing remedial actions.	Senior management meetings to drive performance across each franchise, function and region.	Defines portfolio allocation principles, reviewing and challenging current shape of portfolio, identifying gaps and opportunities and re-prioritising segments and geographies.	Reviews compliance matters and country business unit or function compliance reports.

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Finance & Banking Committee	Disclosures Committee	Mergers & Acquisitions Investment Committee	IT Governance Board
Approves banking and treasury matters, guarantees, Group structure changes relating to mergers, acquisitions and disposals.	Approves release of communications to investors and Stock Exchanges.	Oversees Corporate Development Strategy, monitors status of transactions and approves various stages in merger, acquisition and disposal process.	Oversees IT and cyber security.
Diversity & Inclusion Council	Global Benefits Committee	Health, Safety & Environment Committee	
Implements strategies to promote diversity and inclusion.	Oversees all policies and processes relating to pensions and employee benefit plans.	Oversees health, safety and environmental matters.	

LEADERSHIP

Responsibilities of the Board Board timetable 2018

	January	Early February 2017 Preliminary Results	Late February 2017 Financial Statements	April Annual General Meeting	May Q1 2018
STRATEGY					
– Approving the Group strategy including major changes to corporate and management structure.	Approved Strategic Plan for 2018-2020	Reviewed capital allocation policies			
– Approving acquisitions, mergers, disposals, capital transactions in excess of \$50 million.	Approved 2018 Budget	Reviewed report on post acquisitions reviews			
– Setting priorities for capital investment across the Group.					
– Approving annual budget, financial plan, three-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.

Reviewed financial performance

Reviewed financial performance

Received update on European business

Received updates on global operations

- 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.

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.

Approved Preliminary
Announcement 2017

Considered payment of
final dividend

Approved the:
Annual Report for
2017

Notice of the
Annual General
Meeting

Sustainability Report
2017

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

Approved Q1
2018 Trading
Report

– Approving the
Sustainability Report.

– Maintaining
relationships and
continued engagement
with shareholders.

RISK

– Overseeing the
Group’s risk
management
programme.

Approved Annual
Risk Management Report

Reviewed update on
Brexit

– Regularly reviewing
the risk register.

– Overseeing risk
management processes
(see pages 41-49 for
further details).

PROVIDING ADVICE

– Using experience gained within other companies and organisations to advise management both within and between Board meetings on an ad hoc basis.

OTHER MATTERS

Reviewed
Non-Executive
Director Fees

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.

	June	July H1 2018	September Site visit to Berlin	October Q3 Trading Report	December Strategic Planning
Strategy					
– Approving the Group strategy including major changes to corporate and management structure.	Approved re-financing of the revolving credit facility	Considered the Company's organisational design	Update on organisational change		Approved the strategic plan for 2019-2021
– Approving acquisitions, mergers, disposals, capital transactions in excess of \$50 million.		Considered the Company's strategic focus			Approved the budget for 2019
– Setting priorities for capital investment across the Group.					
– Approving annual budget, financial plan, three-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.

Received report from new Chief Executive Officer on first impressions

Reviewed financial performance, operating review and scorecards

Reviewed financial performance and global operations

Reviewed financial performance

Received update on Medical Devices global market

– 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.

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.

Risk

- Overseeing the Group's risk management programme.

- Regularly reviewing the risk

Approved H1 2018 Results Announcement

Considered report on investor and media perspectives

Approved Q3 2018 Trading Report

Reviewed risk management programme as part of strategy review

register.

– Overseeing risk management processes (see pages 41-49 for further details).

Providing Advice

– Using experience gained within other companies and organisations to advise management both within and between Board meetings on an ad hoc basis.

OTHER MATTERS

Approved the terms of the Directors' and Officers' Liability Insurance

Reviewed results of external board effectiveness review and agreed follow up actions

LEADERSHIP

Our approach to stakeholders

EMPLOYEES

The Board regularly takes the opportunity to meet with staff at all levels in the organisation when making site visits across our operations. Regular staff surveys are undertaken, which the Board reviews and follows up on outcomes. The Compliance & Culture Committee reviews certain workplace policies and whistle-blowing incidents, ensuring that appropriate follow up is implemented as necessary. We ensure that when making strategic decisions the impact upon our employees is fully considered.

Actions during 2018

- The Board reviewed and discussed the results of the Culture Survey and focus forums initiated by Namal Nawana, Chief Executive Officer on joining the Company. See page 24–25.
- We actively debated and approved the culture pillars of Care, Collaboration and Courage, which will underpin our purpose and corporate strategy.
- We met with key employees on our site visit to Berlin in September and some of us have undertaken additional site visits and spent time on the road with our sales representatives.
- The Ethics & Compliance Committee reviewed our policies on sexual harassment.
- In making decisions regarding organisational change and the APEX programme, we have considered the impact on employees, ensuring that all are treated fairly and with respect.
- The Chief Executive Officer and senior management hold quarterly webcasts for the workforce, which encourage employee engagement and dialogue.

The Board will continue to consider the impact on employees when making strategic decisions.

We will continue to take opportunities to meet staff at all levels across the organisation when conducting site visits. We plan to visit our Memphis facility in 2019.

The Compliance & Culture Committee (formerly Ethics & Compliance Committee) will assume responsibility for overseeing our corporate culture and workplace policies and will report back regularly to the Board.

In listening to the employee voice, we have decided not to appoint an employee director or to nominate a single designated Non-Executive Director. Instead, we have designated our Compliance & Culture Committee as a whole with the responsibility for engaging with employees. This programme of employee engagement will be developed and implemented during 2019.

The Board will continue to monitor the outcomes from employee surveys and forums.

Actions planned for 2019

- The Board will continue to consider the impact on employees when making strategic decisions.
- We will continue to take opportunities to meet staff at all levels across the organisation when conducting site visits. We plan to visit our Memphis facility in 2019.
- The Compliance & Culture Committee (formerly Ethics & Compliance Committee) will assume responsibility for overseeing our corporate culture and workplace policies and will report back regularly to the Board.
- In listening to the employee voice, we have decided not to appoint an employee director or to nominate a single designated Non-Executive Director. Instead, we have designated our Compliance & Culture Committee as a whole with the responsibility for engaging with employees. This programme of employee engagement will be developed and implemented during 2019.
- The Board will continue to monitor the outcomes from employee surveys and forums.

CUSTOMERS AND SUPPLIERS

The Board receives regular updates at Board meetings from the management team on relationships with our key customers and suppliers and how these relationships are evolving as we respond to different market conditions and environments. We also take the opportunity to meet with key customers during our site visits.

Actions during 2018

- As part of our country visit to Germany, we visited La Charité Hospital in Berlin, which is the largest University hospital in Germany. We met with surgeons who used our products and also the Chief Executive who outlined some of the challenges in the German market.
- A number of us accompanied sales representatives in the UK, US and Switzerland as they met with customers and surgeons who used our products.
- During the course of the year, we received management updates on different areas of the business. These included presentations on the management of our supply chain, and the changing market environment and expectations from our customers.

The Board will continue to receive management updates on our customers and suppliers.

We will meet with customers and surgeons when we visit our Memphis facility.

The Compliance & Culture Committee will assume responsibility for overseeing relationships with our key stakeholders including customers and suppliers.

Actions planned for 2019

- The Board will continue to receive management updates on our customers and suppliers.
 - We will meet with customers and surgeons when we visit our Memphis facility.
 - The Compliance & Culture Committee will assume responsibility for overseeing relationships with our key stakeholders including customers and suppliers.
-

INVESTORS

The Board meets with retail investors at the Annual General Meeting and responds to letters and emails from shareholders throughout the year. Members of the Board are always happy to engage with investors, if they have matters they wish to raise with the non-executive team. The Chair and other Board members report back to the Board following their meetings with investors. A short report on our major shareholders and any significant changes in their holdings since the previous meeting is reviewed at each Board meeting. Copies of the analyst reports on the Company and its peers are also circulated to Directors.

Actions during 2018

- The Executive Directors held 124 meetings with investors representing 43.8% of the Company's share capital. They discussed a range of topics including strategy, performance and organisational structure.
- The Chair, Roberto Quarta, held 7 meetings and telephone calls with investors holding approximately 12.6% of the Company's share capital. They discussed a range of topics including the performance of the Company, the appointment of Namal Nawana as our new Chief Executive Officer, our Strategy, the structure of the Board and succession planning at Board and Executive level.
- The Chair of the Remuneration Committee, Angie Risley reached out to our top 20 shareholders holding 44% of the company's shares and received responses from 9 shareholders collectively holding 17.1% of the company's share capital in connection with Graham Baker's pay following his increased responsibility for IT and Global Business Services. See page 85 for further details.

The Board will continue to receive regular updates at Board meetings on management and Chair meetings with investors and will review regular analyst reports.

The management team and the Chair and Non-Executive Directors will continue to engage with shareholders. If you have matters to raise with the non-executive team, please contact the Company Secretary.

Actions planned for 2019

- The Board will continue to receive regular updates at Board meetings on management and Chair meetings with investors and will review regular analyst reports.
- The management team and the Chair and Non-Executive Directors will continue to engage with shareholders. If you have matters to raise with the non-executive team, please contact the Company Secretary.

GOVERNMENTS AND REGULATORS

In many countries, our principal customers are governments, who purchase our products for their national health systems. It is important that we maintain good relationships with governments so that we continue to develop cost efficient solutions to their national healthcare issues. We operate in a heavily regulated industry and our businesses across the world are regulated by many different authorities in different jurisdictions. Our Compliance & Culture Committee has for a number of years overseen our relationships with our key regulators, particularly in areas of ethics, compliance and quality.

Actions during 2018

- The Compliance & Culture Committee received regular reports from the Quality and Regulatory function on regulatory activities and the results of regulatory inspections.
- The Compliance & Culture Committee received regular reports from the Legal & Compliance function on the activities of key agencies relating to ethics and compliance matters.
- The Board received regular updates from the business areas on the pricing challenges faced by the business when dealing with governments operating with limited financial resources.
- The Board and the Audit Committee received regular updates relating to the progress towards Brexit and management plans to manage the transition as smoothly as possible.

The Compliance & Culture Committee will continue to oversee relationships between the Company and our regulators.

The Board and the Audit Committee will continue to monitor management preparations for Brexit.

Actions planned for 2019

- The Compliance & Culture Committee will continue to oversee relationships between the Company and our regulators.
- The Board and the Audit Committee will continue to monitor management preparations for Brexit.

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Leadership

Responsibilities of the Board

BOARD AND COMMITTEE ATTENDANCE

		Board	Committee		Nominations & Governance	Compliance & Culture
			Audit	Remuneration		
Total meetings		10	8	5	4	4
	Appointed					
Roberto Quarta ¹	December 2013	10/10	–	5/5	3/4	–
Olivier Bohuon ²	April 2011	5/5	–	–	–	–
Graham Baker	March 2017	10/10	–	–	–	–
Vinita Bali	December 2014	10/10	–	5/5	–	4/4
Ian Barlow ³	March 2010	10/10	7/8	–	4/4	4/4
Virginia Bottomley	April 2012	10/10	–	5/5	4/4	–
Roland Diggelmann ⁴	1 March 2018	7/7	5/6	–	–	–
Erik Engstrom	January 2015	10/10	8/8	–	–	–
Robin Freestone	September 2015	10/10	8/8	5/5	–	2/2
Michael Friedman	April 2013	10/10	–	–	–	4/4
Namal Nawana ⁵	7 May 2018	5/5	–	–	–	–
Marc Owen	October 2017	10/10	8/8	–	–	3/3
Joseph Papa ⁶	August 2008	4/4	3/3	2/2	–	2/2
Angie Risley	September 2017	10/10	–	5/5	–	–

¹Roberto Quarta missed one Nomination & Governance Committee meeting on 11 April 2018 because of another commitment.

²Olivier Bohuon retired from the Board on 7 May 2018.

³Ian Barlow missed one Audit Committee meeting on 11 April 2018 in order to attend a funeral.

⁴Roland Diggelmann was appointed on 1 March 2018. He missed one Audit Committee meeting on 24 July 2018 because of another commitment scheduled before his appointment.

⁵Namal Nawana was appointed on 7 May 2018 and attended all his scheduled meetings to 31 December 2018.

⁶Joseph Papa retired from the Board at the Annual General Meeting on 12 April 2018.

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.

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 15 February 2019.

Each Director has a duty under the Companies Act 2006 to avoid a situation in which they 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, eight 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. Namal Nawana is an independent Director of Hologic Inc. Namal discussed his external role with the Chair prior to his appointment and the Chair was satisfied that he had the capacity for the time commitment required. Suitable arrangements were put in place when reaching a settlement with Hologic related to historical intellectual property litigation to ensure that Namal was not party to any of the negotiations or discussions, which could have given rise to an actual conflict.

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.

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 172.

Board effectiveness review

The Board effectiveness review in 2018 was externally facilitated by Dr Tracy Long of Boardroom Review. Dr Long interviewed each member of the Board and the Company Secretary, reviewed minutes, Board papers and other Board documents, and attended and observed the Board and Committee meetings held in October 2018. She then prepared a report summarising her findings, which she presented to the Board for discussion in December.

FINDINGS

Overall she observed that the Board had many strengths, was effective with a diversity of perspectives and was an open supportive environment. It was led by a strong Chair, the Chief Executive Officer and Chief Financial Officer were both highly regarded and recent appointments had strengthened the Board's domain knowledge. Finance, risk and governance controls were working well and corporate culture was openly discussed at Board level.

RECOMMENDATIONS

She did note however that there were challenges ahead, given the number of initiatives underway across the Company to lift performance, the recent appointment of a new Chief Executive Officer, a refreshed management team and the development of new Strategic Imperatives, Purpose and Culture Pillars. There would be additional work for the Board in coming months to get behind the new strategy and develop a shared perspective on the future strategy and appetite for risk.

The Board accepted the recommendations and an action plan is being developed to address them.

RECOMMENDATION 1

– The Board will need to ensure that it continually reviews and ensures alignment of its appetite for risk against the changing landscape and revised Strategic Imperatives, particularly as the Company continued to evolve. This will require continued monitoring of Board composition and succession planning.

RECOMMENDATION 2

– Performance management will need to evolve to monitor alignment with the new strategy, with an increased emphasis on a globally consistent culture and purpose.

RECOMMENDATION 3

– The workload, composition and support for the Board Committees will be reviewed to ensure a more even balance of workload and greater diversity on each Committee.

RECOMMENDATION 4

– The Chair and Chief Executive Officer will agree shared priorities for Board site visits at the beginning of each year, so that individual and group site visits could be arranged within these agreed parameters rather than on an ad hoc basis.

The areas for attention identified in the 2017 review have been addressed as follows:

ACTIONS IDENTIFIED

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

ACTION TAKEN

During the year, the Board and Committee calendar for the year has been reviewed and updated and a revised rolling calendar has been prepared for 2019, aligned to the new Group strategy and the updated Strategic Imperatives.

The Board site visit to Berlin in September 2018 incorporated meetings with the German management team and a visit to

local hospitals to give us a deeper understanding of our markets, our customers and 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 our strategy, and lessons learned from our successes and shortfalls.

The reviews in 2019 and 2020 will be facilitated internally and led by the Senior Independent Director and the Company Secretary. The 2021 review will also be facilitated externally.

La Charite, the largest university hospital in Germany to meet with surgeons and hospital staff. This helped us gain a deeper understanding of the views and needs of our customers.

During the year, we have evolved the way reports on performance are presented to the Board. Going forward, performance reports will be aligned with the new Strategy and Strategic Imperatives.

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Leadership

Board development

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 effective 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 Chair regularly reviews the development needs of individual Directors and the Board as a whole.

The following development sessions covering the Smith & Nephew business and wider market issues were held during the year:

June	September	October	December
2018 PROGRAMME			
The Board received an overview from the new Executive Officer on his impressions of the Company and his proposals for a new organisational structure.	Visit to Germany to meet with our local management team and to visit La Charité, the largest university hospital in Germany and one of our significant customers. The Board received presentations from local surgeons and members of the hospital's executive team about the challenges faced in the German healthcare market and role played by Smith & Nephew.	Presentation from Deloitte LLP to the Remuneration Committee on the changes to be made to the role of the Committee in light of the new UK Corporate Governance Code. Presentation by the Company Secretary to the Audit Committee/Nomination & Governance Committee on the changes required by the UK Corporate Governance Code to the roles and structure of the Board and its Committees. Presentation to the Board by McKinsey on the current environment and trends in the Medical Devices industry.	Presentations from the entire Executive team as part of the Board's annual Strategy Review, covering the whole business.
	The Board received updates from new members of the		

Executive team on their first impressions on joining the Company and their plans for the EMEA business, Global Operations and Quality and Regulatory Assurance.

The Board received updates from the Executive team on Investor and Media coverage, and the results of the culture survey and focus groups carried out earlier in the summer.

INDUCTION PROGRAMME FOR NEW DIRECTORS

- During 2018, Roland Diggelmann joined the Board. He and Angie Risley and Marc Owen continued to receive tailored induction programmes relevant to their skills and experiences and their roles on the Board. These induction programmes included:
 - 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 in UK, US and Switzerland to get a feel of how our research and manufacturing operations are run;
 - Opportunities to accompany our sales representatives in the US 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 Deloitte LLP, 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.
-

Nomination & Governance Committee report

Ensuring the Board evolves to align with the new Strategic Imperatives and with the developing external regulatory environment.

Membership

	Member from	Meetings attended
Roberto Quarta (Chair) ¹	April 2014	3/4
Ian Barlow ²	April 2014	4/4
Erik Engstrom ³	April 2019	N/A
Robin Freestone ³	April 2019	N/A
Virginia Bottomley	April 2014	4/4

¹Roberto Quarta missed the meeting in April because of a conflicting commitment.

²Ian Barlow will be retiring from the Board and the Committee at the Annual General Meeting to be held on 11 April 2019, having completed nine years' service.

³Erik Engstrom and Robin Freestone will join the Nomination & Governance Committee on 11 April 2019.

The terms of reference for the Nominations & Governance Committee describe the role and responsibilities of this Committee more fully and can be found on our website at www.smith-nephew.com.

Early February March April October

BOARD COMPOSITION

– Reviewing the size and composition of the Board.	Approved the re-appointment of Directors who had completed three or six years' service and the annual	Considered candidates for the role of Chief Executive Officer and agreed to recommend to the Board the	Reviewed the composition of the Board and agreed to appoint Robin Freestone as Senior Independent Director
– Overseeing Board succession plans.			

- | | | | |
|--|---|--|---|
| <ul style="list-style-type: none"> – Recommending the appointment of Directors. – Monitoring Board diversity. | <ul style="list-style-type: none"> appointment of Directors serving in excess of six years. Discussed progress on search for a new Chief Executive Officer. | <ul style="list-style-type: none"> appointment of Namal Nawana. | <ul style="list-style-type: none"> to replace Ian Barlow who would be retiring from the Board at the Annual General Meeting in 2019. |
| <p>CORPORATE GOVERNANCE</p> | | | |
| <ul style="list-style-type: none"> – Overseeing 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. | <ul style="list-style-type: none"> Reviewed and approved the Schedule of Matters Reserved to the Board and the terms of reference of the Board Committees. | <ul style="list-style-type: none"> Reviewed current governance trends in the UK and particularly the changes likely to be proposed in the UK Corporate Governance Code. | <ul style="list-style-type: none"> Reviewed the annual cadence of Board and committee meetings. Considered the implications of the UK Corporate Governance Code 2018 and in particular the expanded role of the Board relating to corporate culture and relationships with stakeholders and agreed that the remit of the Ethics & Compliance Committee be expanded to undertake some of these responsibilities on behalf of the Board. |
-

NOMINATION & GOVERNANCE COMMITTEE REPORT continued

In 2018, we held four meetings. In addition to members of the Committee, the Company Secretary, Chief Executive Officer and Chief Human Resources Officer also attended all or some of the meetings. Other Non-Executive Directors were invited to join the meetings to discuss the search for a new Chief Executive Officer.

Further matters were resolved by written resolution including the appointment of Roland Diggelmann.

Since the year end, we have also discussed the future structure of the Board and its Committees and completed our year end governance processes.

APPOINTMENT OF CHIEF EXECUTIVE OFFICER

During the early part of the year, the Committee continued its search for a new Chief Executive Officer to replace Olivier Bohuon who had announced his intention to retire by the end of 2018. The Committee recommended the appointment of Namal Nawana, who joined the Company as Chief executive Officer in May 2018. Namal brings a wealth of experience of the international medical devices industry to his role. The Nomination & Governance Committee was advised by Russell Reynolds on this appointment. Russell Reynolds also advises the Company on other executive recruitment and appointments.

NON-EXECUTIVE DIRECTORS

The Committee has reviewed the composition of the Board and its Committees to ensure that it evolves to align with the new Strategic Imperatives and with the developing external regulatory environment.

The Committee also recommended the appointment of Roland Diggelmann as an additional Non-Executive Director who joined the Board in March 2018. Roland has many years' experience in the Medical Devices industry. Russell Reynolds advised the Committee on this appointment.

Ian Barlow will be retiring from the Board and from his position as Senior Independent Director at the Annual General Meeting to be held on 11 April 2019, following completion of nine years' service as Non-Executive Director and until 2017 as Chairman of the Audit Committee and then latterly as Senior Independent Director. The Committee recommended to the Board that Robin Freestone be appointed Senior Independent Director in Ian's place at the conclusion of the Annual General Meeting, subject to his re-appointment by shareholders.

Robin will continue to Chair the Audit Committee, but the Committee will undertake a search for an additional Non-Executive Director with recent and relevant financial experience who could in time succeed Robin as Chair of the Audit Committee. When considering candidates for this role, the Committee will be mindful of building a diverse Board and will aim to ensure an appropriate balance of genders, ethnicity, backgrounds, skills and experience.

Michael Friedman will also be retiring from the Board and from his position as Chair of the Compliance & Culture Committee at the Annual General Meeting, following the completion of six years' service. He will be succeeded as Chair of the expanded Compliance & Culture Committee by Marc Owen.

Erik Engstrom and Robin Freestone will be joining the Nomination & Governance Committee as additional members in April 2019 after the Annual General Meeting and Virginia Bottomley and Roland Diggelmann will be joining the Compliance & Culture Committee at the same time.

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 homogeneous 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 understanding 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.

During 2018, 25% of our Board were female. With the retirement of Ian Barlow and Michael Friedman in April 2019, this percentage rises to 30%. Looking forward, we are working towards a Board with 33% female representation in line with the Hampton-Alexander Review. From 7 May 2018, 17% of our Board were of non-white ethnicity. This rises to 20% after the Annual General Meeting in April 2019.

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.

SUCCESSION PLANNING

Since the appointment of Namal Nawana as Chief Executive Officer in May 2018, we have initiated substantial changes to our structure to move to a franchise-led model, as described on page 14. Throughout the year, the Board and Nomination & Governance Committee have monitored the consequent changes to the organisational structure and approved appointments to key leadership positions. Individual Directors have acted as a sounding board for the executive team when considering succession plans in key areas. Given the level of change during 2018, this will be a continued focus of the Nomination & Governance Committee during 2019.

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. 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 following matrix. We review this matrix regularly to ensure that it is refreshed to meet the changing needs of the Company.

CEO	Financial	International	Healthcare/ Medical Devices	Emerging market
Four members of the Board are either current or recent CEOs	Two members of the Board have recent and relevant financial experience	Seven members of the Board have international experience	Six members of the Board have different levels of experience within the Healthcare industry	Two members of the Board have Emerging Market experience
UK Governance	Remuneration	Gender	Ethnic	Other
Six members of the Board have considerable experience of working in a UK listed environment and four members of the Board have experience of the US listed environment	Five members of the Board have Remuneration Committee experience within a UK listed context	Nine members of the Board are male and three are female	Ten members of the Board are white and two are of Asian ethnicity	Various Board members bring experiences in a variety of fields including customer focus, investment markets, government affairs, digital and corporate social responsibility

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. 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 also took the opportunity of reviewing whether the annual cadence of our Board and Committee meetings was appropriate for the work we need to undertake. As a result of this review, we have changed the physical October meeting to approve the third quarter trading figures to a half day Board telephone call. We have also introduced additional monthly Board update calls for those months when we do not meet physically and will be introducing separate site visits for Non-Executive Directors to meet employees and customers.

We also considered how we would implement the requirements of the 2018 UK Corporate Governance Code and agreed that the Remuneration Committee would retain responsibility for provisions relating to executive pay and pay matters generally. This is discussed further on pages 84-85. We also agreed that the remit of the new Compliance & Culture Committee would be expanded to cover responsibility for overseeing corporate culture and relationships with stakeholders on behalf of the Board. The revised remit of the Compliance & Culture Committee is discussed on

pages 74–75 and our approach to listening to the voice of our employees and other stakeholders is discussed on pages 66–67. We have noted the three options set out in the 2018 UK Corporate Governance Code for listening to the Employee Voice and have determined that this will be the responsibility of the Compliance & Culture Committee as this is too important an issue to fall to one Non-Executive Director.

LOOKING FORWARD

During 2019 our focus will include:

- > Search for an additional Non-Executive Director with recent and relevant financial experience to serve on the Audit Committee.
- > Monitoring the implementation of the revised Board and Committee structure to ensure that the Company complies with the UK Corporate Governance Code or explains why not.

Roberto Quarta

Chairman of the Nomination & Governance Committee

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Compliance & Culture Committee report (formerly Ethics & Compliance Committee)

Broadening our scope to oversee culture in addition to our focus on compliance and quality.

Membership

	Member from	Meetings attended
Michael Friedman (Chair) ¹	August 2014	4/4
Vinita Bali	April 2015	4/4
Virginia Bottomley ²	April 2019	N/A
Ian Barlow ³	October 2014	4/4
Roland Diggelmann ⁴	April 2019	N/A
Marc Owen ⁵	1 March 2018	3/3
Joseph Papa ⁶	August 2008	2/2
Robin Freestone	24 July 2018	2/2

¹Michael Friedman will retire from the Board and the Committee at the Annual General Meeting on 11 April 2019.

²Virginia Bottomley will join the Committee on 11 April 2019.

³Ian Barlow will retire from the Board and the Committee on 11 April 2019.

⁴Roland Diggelmann will join the Committee on 11 April 2019.

⁵Marc Owen joined the Committee on 1 March 2018.

⁶Joseph Papa retired from the Board and the Committee on 12 April 2018.

	February	April	July	October
ETHICS & COMPLIANCE				
– Overseeing ethics and compliance programmes, strategies and plans.	Noted the progress made on the Global Compliance Programme Plan for 2017 and noted the plan of action for	Reviewed the ethics and compliance training programmes in place across the Group.	Noted progress on the 2018 Global Compliance Plan of Action.	Received Ethics & Compliance update in new format and noted insights from various aspects of Global Compliance Programme.

- Monitoring ethics and 2018. compliance process improvements and enhancements. Reviewed significant findings from monitoring, auditing and progress on Corrective and Preventative Actions.
- Assessing compliance performance based on monitoring, auditing and internal and external investigations data. Reviewed significant findings from monitoring auditing, and progress on Corrective and Preventative Actions.
- Reviewing allegations of significant potential compliance issues.
- Receiving reports from the Group’s Ethics & Compliance Committee meetings and from the Chief Legal and Compliance 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. Reviewed various quality metrics. Reviewed various quality metrics and approved the Global Quality Plan for 2018, noting the additional work to be done to implement the EU MDR. Reviewed various quality metrics including the results of inspections by the FDA and Notified Bodies, progress on handling complaints and in preparing for the EU MDR. Received Quality and Regulatory report in updated format from newly appointed Chief Quality and Regulatory Affairs Officer, noting status of various Quality and Regulatory metrics and initiatives.
- Receiving and assessing regular functional reports and presentations from the Chief Quality and Regulatory Affairs Officer, or the SVP Quality Assurance.

OTHER MATTERS

- February
Reviewed the sexual harassment policies and procedures in place across the Group. As a follow up to the February meeting, reviewed the circumstances and actions taken to address the sexual harassment allegations made in the year.

The Terms of Reference of the Compliance & Culture Committee describe the role and responsibilities more fully and can be found on our website at www.smith-nephew.com.

In 2018, we held four physical meetings. Each meeting was attended by all members of the Committee. The Company Secretary, the Chief Legal and Compliance Officer and the Chief Quality and Regulatory Affairs Officer or SVP, Quality Assurance also attended all or part of the meetings by invitation.

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. 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 Chief Quality and Regulatory Affairs Officer, or the SVP Quality Assurance.

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. We also monitored the work being undertaken to help our manufacturing sites to prepare for future inspections.

We reviewed the results of quality audits undertaken during the year, noted 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. 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 Legal and Compliance 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 for employees and sales agents, 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.

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.

During the year, we expanded our remit and reviewed the policies and procedures we have in place to handle claims of sexual harassment.

LOOKING FORWARD

The Board and the Committee have considered the UK Corporate Governance Code 2018 and have decided to expand the role of the Committee to cover a broader focus. Whilst oversight of our Ethics & Compliance programme will continue to remain a key focus for us and we will monitor and assess quality and regulatory issues, we will also oversee culture across the organisation and relationships with our key stakeholders. We will develop the mechanism for ensuring that the Board listens to the employee voice and will oversee the Sustainability Programme.

Our focus for 2019 will include:

- > Develop a programme to enable the Board to monitor and assess the corporate culture.
- > Develop a programme to enable the Board to engage with employees, building on existing processes within the Company.
- > Ensure oversight of the Company's Sustainability programme and relationships with key stakeholders.

This will be my final report as Chair of this Committee, as I shall be retiring from the Board at the Annual General Meeting. I should like to thank my colleagues on the Committee and particularly Marc Owen who will be succeeding me as Chair of the Committee and overseeing its expanded focus on culture, the employee voice and stakeholders.

Michael Friedman

Chair of the Compliance & Culture Committee

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Audit Committee report

2018 was my first full year as Chair of the Audit Committee. I have overseen a busy schedule – with the Committee meeting eight times during the year.

Membership

	Member from	Meetings attended
Robin Freestone (Chair) ¹	September 2015	8/8
Ian Barlow ^{1,2}	May 2010	7/8
Roland Diggelmann ^{3,4}	March 2018	5/6
Erik Engstrom	January 2015	8/8
Mark Owen	October 2017	8/8
Joseph Papa ⁵	February 2011	3/3

¹Designated financial experts under the SEC Regulations or recent and relevant financial experience under the UK Corporate Governance Code.

²Ian Barlow missed one Audit Committee meeting on 11 April 2018.

³Roland Diggelmann joined the Audit Committee on 1 March 2018.

⁴Roland Diggelmann missed one Audit Committee meeting on 24 July 2018.

⁵Joseph Papa retired from the Board and Audit Committee at the Annual General Meeting on 12 April 2018.

In addition to discharging its role in accordance with its terms of reference, the Committee has met its commitments to provide assurance in respect of various non-routine matters. Areas of scrutiny for the Committee in 2018 have included: the progression of NAPO, (our SAP Enterprise Resource Planning migration in North America); top risks identified in the 2017 Annual Report such as Cyber Security; Brexit readiness; and the Accelerating Performance and Execution (APEX) programme. In 2018 the Committee oversaw the adoption of two accounting standards, IFRS 15 Revenue from contracts with customers and IFRS 9 Financial Instruments. A detailed impact assessment of the application of IFRS 15 was undertaken with the conclusion being that there was no significant impact on the timing and recognition of revenue. The main impact on adoption of IFRS 9 has been the implementation of the expected credit loss methodology for the calculation of the loss allowance for trade receivables. This resulted in an additional loss allowance of \$14 million being recognised on 1 January 2018. With regard to IFRS 16 Leases, the Committee considered the application of exemptions, estimated impact, transition preparations (including the implementation of a

new lease accounting software solution) and transition readiness. IFRS 16 will be adopted on 1 January 2019 with no restatement of comparatives.

In May 2018 we welcomed our new Chief Executive Officer, Namal Nawana. Under Namal's leadership, Smith & Nephew has established its new strategy and organisational structure. That will provide the context for our focus of activity for 2019 – particularly as it will form the backdrop for our risk assessment. Roland Diggelmann joined the Audit Committee in March 2018 where his experience and expertise enables him to provide appropriate challenge to information presented at meetings by the Executive. Ian Barlow will be standing down as a member of the Board after the AGM on 11 April. He has served as member of the Committee since 2010 (including seven years as Chair) and has been the Senior Independent Director since 2017. I should like to take this opportunity to thank Ian for his valuable contribution and wise counsel during his tenure.

KPMG have now completed their fourth year's audit and continue to provide robust challenge. We have negotiated fees that will continue to be reviewed for good market practice. We have also agreed arrangements for rotation of the senior partner in accordance with recommendations set out in the Financial Reporting Council's (FRC) Guidance for Audit Committees 2016 and as required by the Securities Exchange Commission (SEC). Finally, we note the positive comments received from the FRC following its review of KPMG's audit of Smith & Nephew's financial statements for 2017.

Our focus for 2019 will include:

- > The next phase of the APEX programme.
- > Ensuring compliance with new leasing standard IFRS 16.
- > Risk management process – aligned to the new strategy and organisational structure.
- > Continuing to provide assurance on the effectiveness of managing the risks associated with Cyber Security.
- > Ensuring that we are compliant with additional governance and reporting requirements coming into effect for 2019 – such as the revised UK Corporate Governance Code.

Robin Freestone

Chair of the Audit Committee

The Terms of Reference of the Audit Committee describe the role and responsibilities more fully and can be found on our website at www.smith-nephew.com.

SIGNIFICANT MATTERS RELATED TO THE FINANCIAL STATEMENTS

We considered the following key areas of judgement in relation to the 2018 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 inventory makes up approximately 60% of the Group total 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 18% at 31 December 2018 (19% as at 31 December 2017). 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 and Compliance 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 metal-on-metal hip products of \$192 million as of 31 December 2018. 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 claim. The provisions for legal matters have increased by \$27 million during the year, primarily due to an increase in the metal-on-metal provision. There have been some smaller movements from other

cases having been resolved. We have determined that the proposed levels of provisioning at year end of \$217 million included within 'provisions' in Note 17.1 in 2018 (\$190 million in 2017) 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 concluded that the carrying value of these assets 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 and it is Group policy to submit its tax returns to the relevant tax authorities as promptly as possible. At any given time, the Group is involved in disputes and tax audits and will have a number of tax returns potentially subject to audit. 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 tax provision whenever necessary. The ultimate tax liability may differ from the amount provided depending on factors including 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. 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.

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AUDIT COMMITTEE REPORT continued

	Early February Preliminary Announcement	Late February Financial Statements	April	May 2018 Q1 Trading Report
FINANCIAL ACCOUNTING AND REPORTING				
– Reviewing significant financial reporting judgements and accounting policies and compliance with accounting standards.	Endorsed 2017 results and Preliminary announcement Report from KPMG on 2017 results Reviewed draft 2017 Annual Report including report of the Audit Committee	Approved the Annual Report and Accounts for 2017 including report of the Audit Committee – confirming fair, balanced and understandable Report from KPMG on 2017 statements – Unqualified Opinion Approved letter of representation for 2017 Reviewed S302 and S906 certifications Confirmed Going Concern and Viability Statement	Debrief of Annual Report process and timetable for 2018 Approved Senior Finance Officers Code of Ethics Reviewed summary of Company audits	Reviewed and endorsed 2018 Q1 Trading Report and announcement Approved the Company’s policy and report on Conflict Minerals for submission to NYSE
– Ensuring the integrity of the financial statements and their compliance with UK and US statutory requirements.	Assessed compliance with UK and US governance 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
AUDIT

<p>– Agreeing Internal Audit plans and reviewing reports of Internal Audit work.</p>	<p>Reviewed year end Report</p>	<p>Reviewed effectiveness of Internal Audit</p>	<p>Reviewed progress</p>
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– 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.

RISK
MANAGEMENT

<p>– 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.</p>	<p>Risk Management Update</p>	<p>Confirmed effective system of risk management in place and approved the Viability Statement</p>
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– 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.

– Overseeing risk management processes (see pages 40–49 for further details).

– Regularly reviewing the risk register.

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.

Considered Sarbanes-Oxley (Sox) and MAPs Update

Reviewed effectiveness of Internal Controls over financial reporting

Considered Sarbanes-Oxley (Sox) and MAPs Planning 2018

– Reviewing the operation of the Group’s risk mitigation processes and the control environment over financial risk.

FRAUD & WHISTLE-BLOWING

– Receiving reports on the

Reviewed Internal Audit Report on Fraud

processes in place to prevent fraud and to enable whistle-blowing and Whistle-blowing

– If significant, receive and review reports of potential fraud or whistle-blowing incidents.

– Reviewed Internal Audit Report on Fraud.
EXTERNAL AUDITOR

– Overseeing the Board's relationship with the external auditor. Confirmed independence of KPMG

Reviewed effectiveness and independence and concluded their effectiveness

Endorsed External Audit Plan

Approved 2017 fee overruns

Approved external auditor fees for 2017

– 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.

OTHER MATTERS

Endorsed NAPO processing and

Approved consultancy fees to external advisors Treasury Update

scheduling plan

Cyber Security

Approved Audit
Committee's TOR

Project reports

including Apex

China Channel
Management

	July 2018 H1 Results	September	October 2018 Q3 Trading Report	December
FINANCIAL ACCOUNTING AND REPORTING				
– Reviewing significant financial reporting judgements and accounting policies and compliance with accounting standards.	Reviewed and endorsed H1 results and announcement		Reviewed and endorsed Q3 Trading Report and announcement	Reviewed accounting matters for 2018
– Ensuring the integrity of the financial statements and their compliance with UK and US statutory requirements.	Report from KPMG on H1 results		Clarified MDR policy	Considered and approved critical accounting policies and judgements in advance of 2018 year end
– Ensuring the Annual Report and Accounts are fair, balanced and understandable and recommending their adoption by the Board.	Approved letter of representation for H1 2018		New reporting and regulatory requirements update	Reviewed preparation work for adoption of IFRS 16
– Monitoring announcements relating to the Group’s financial performance.				Approved plans for delivery of the Annual Report 2018
INTERNAL AUDIT				
– Agreeing Internal Audit plans and reviewing reports of Internal Audit work.		Reviewed progress		Reviewed Progress and approved Charter and 2019 Plan
– 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.				
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.	Risk Management Update		Risk Management Update	Risk Management Update

– 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

– Overseeing risk management processes (see pages 40–49 for further details).

– Regularly reviewing the risk register.

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.

Considered Sarbanes-Oxley (Sox) and MAPs progress

Considered Sarbanes-Oxley (Sox) and MAPs progress

– Reviewing the operation of the Group’s risk mitigation processes and the control environment over financial risk.

FRAUD & WHISTLE-BLOWING

– Receiving reports on the processes in place to prevent fraud and to enable whistle-blowing.

Reviewed Internal Audit Report on Fraud

Reviewed Internal Audit Report on Fraud and Whistle-blowing

– If significant, receive and review reports of potential fraud or whistle-blowing incidents.

– Reviewed Internal Audit Report on Fraud

EXTERNAL AUDITOR

– Overseeing the Board’s relationship with the external auditor.

Approved Engagement letter for 2018

KPMG Fee Schedule 2018

Results of FRC Review of KPMG

– Monitoring and reviewing the independence and performance of the external auditor and evaluating their effectiveness.

Noted partner rotation arrangements

– Making recommendations to the Board for the appointment or

re-appointment of the external auditor.

– Monitoring and approving the external auditor's fees.

OTHER MATTERS

Cyber Security Update

Update on NAPO

Tax Update

Project reports including APEX

Cyber Update

APEX Update

Tax Update/Strategy

Cyber Security

AUDIT COMMITTEE REPORT continued

OTHER MATTERS RELATED TO THE FINANCIAL STATEMENTS

Regular private meetings have taken place between the Audit Committee and the External auditor (KPMG) and the Audit Committee and the Group Head of Internal Audit.

As well as the identified significant matters, other matters that the Audit Committee considered during 2018 were:

Business combinations

During 2018, we considered and concurred with management that there had been no changes to the provisional fair values recognised in the 2017 acquisition of Rotation Medical, Inc.

Post Retirement Benefits

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.

Since the year end

Since the year end we have also reviewed the results for the full year 2018, the preliminary announcement, Annual Report and Accounts, for 2018 and have concluded that they are fair, balanced and understandable. 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 12–13, risks and the key performance indicators and their link to the strategy.

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 four 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 2018 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 Board in the UK 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 2018 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 11 April 2019 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.

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 recognises 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.

Any pre-approved aggregate, individual amounts up to \$25,000 may be authorised by the Group Treasurer 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 2018, which were approved by the Chairman of the Audit Committee:

	2018	2017
	\$ million	\$ million
Tax fees and compliance services Assistance with tax compliance in Singapore only	–	0.1

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 2018 is 0.00. The ratio of non-audit fees to audit fees for the year ended 31 December 2017 was 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:

	2018	2017
	\$ million	\$ million
Audit fees	6.0	4.4
Audit-related fees	–	–
Total	6.0	4.4

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 Group Head of Internal Audit, consists of appropriately qualified and experienced employees. Third parties may be engaged to support audit work as appropriate.

The Group Head of 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 53 risk based audits and reviews across the Group. These included Financial and Operational Market based reviews covering the EMEA, APAC, US and Latam Regions; Global Operations, including manufacturing and supply chain; IT and various Programme Assurance reviews ranging from the implementation of SAP across the North American Business to MDR preparedness. Key issues noted during reviews included the need to better control user access to some systems, also the need to improve internal controls in a number of smaller markets. Management has taken swift action to implement Internal Audit's recommendations.

A periodic review of the Internal Audit function is undertaken by an independent external consultant, in accordance with the guidelines of the Institute of Internal Auditors. In 2018 KPMG completed an ISA 610 review of the function and this concluded satisfactorily. Finally, the performance of the function is assessed using a structured questionnaire, 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 December 2018, 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, July, September and December. We approved the Risk Management Programme for 2018 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.

The Risk Management programme in 2018 followed the new risk management policy and manual rolled out across the Company in 2017. This programme combines a "bottom up" approach (whereby risks are identified within business areas by local risk champions working with their leadership teams), with a top-down approach (when the Executive Committee meets as the Risk Committee to consider the risks facing the Group at an enterprise level).

Throughout the year, the Audit Committee maintained oversight of this programme. We reviewed the principal risks identified and the heat maps prepared by management showing how these risks were being managed. We considered those risks where the risk profile was changing particularly political and economic risks as a consequence of Brexit. We also reviewed the deep dives undertaken by the Group Risk team, which looked more closely at the risks impacting certain business areas.

AUDIT COMMITTEE REPORT continued

Since the year end, we have reviewed a report from the Group Head of 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 2018 and up to the date of approval of this Annual Report was effective. Work will continue in 2019 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 50–51.

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 42–47.

The financial position of the Group, its cash flows, liquidity position and borrowing facilities are described on page 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 and group function is responsible for the establishment, maintenance and review of effective financial controls within their business unit or function.
 - The Group's IT organisation is responsible for the establishment of effective IT controls within the core financial systems and underlying IT infrastructure.
 - The Financial Controls & Compliance Group has responsibility for the review of the effectiveness of controls operating in the countries, functions and IT organisation, either by performing testing directly or reviewing testing performed in-country.
 - The Group Finance Manual sets out financial and accounting policies. The Group's Minimum Acceptable Practices (MAPs) have been further enhanced during 2018 by simplifying and clarifying the requirements as well as broadening their scope and incorporating the core financial controls. 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 & Compliance Group 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 our core financial controls globally and merging with the MAPs. In 2019, there will be a focus on implementing a technology solution to facilitate the operation and testing of 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 & Compliance, Taxation and Treasury functions.
 - The Audit Committee reviews regular reports from the Financial Controls & Compliance Group 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, or the Finance and Banking 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 is reviewed by the Audit Committee on behalf of the Board.
- The Audit Committee reviews the Group whistle-blower procedures to ensure they are effective.
- The Audit Committee received and reviewed a report on the progress of the Finance Transformation during 2018 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 2018 and up to the date of approval of this Annual Report. No concerns were raised with us in 2018 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 its Internal Audit function, reviews the adequacy and effectiveness of internal control procedures and identifies any significant weaknesses and ensures these are remediated within agreed timelines. The latest review covered the financial year to 31 December 2018 and included the period up to the approval of this Annual Report. The main elements of this 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 2018. Based upon this evaluation, the Chief Executive Officer and Chief Financial Officer concluded on 21 February 2019 that the disclosure controls and procedures were effective as at 31 December 2018.
- 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 2018 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 2018, 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 2018.

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 substantive amendments to the Code during 2018 or up until 15 February 2019. 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, conducted by Boardroom Review.

The review by the Audit Committee found the following and the below action will be taken during 2019:

Composition	Following retirement of Ian Barlow an additional member with recent and relevant financial experience will be required
Performance & Effectiveness	The Audit Committee is well chaired, with a clear role, an efficient use of time and high quality information

Directors' Remuneration Report

Remuneration Committee report

Our focus in 2019 will be on aligning our remuneration arrangements to the new Strategic Imperatives of the Company

MEMBERSHIP

	Member from	Meetings attended
Angie Risley ¹ (Chair)	September 2017	5/5
Vinita Bali	April 2015	5/5
Virginia Bottomley	April 2014	5/5
Robin Freestone	September 2015	5/5
Joseph Papa ¹ (Former Chair)	April 2011	2/2
Roberto Quarta	April 2014	5/5

¹ Angie Risley was appointed Chair of the Committee on 12 April 2018 replacing Joseph Papa, on his retirement from the Board.

DEAR SHAREHOLDER,

It is a great pleasure to be writing to you for the first time as Chair of the Remuneration Committee. I should like to take the opportunity of thanking my predecessor, Joseph Papa, who was a great support to me during our handover process. The recruitment of Namal Nawana as our new Chief Executive Officer and the consequent changes to his leadership team have given the Committee a full programme during the year. We have also considered the expansion of the role of the Remuneration Committee in the light of revised remuneration regulations and corporate governance reforms. At all times, we have sought to ensure that our pay arrangements support and drive delivery of the strategic aims set out by the Company, while making careful decisions to align pay outcomes with the performance delivered during the period.

Review of 2018 Performance

During the year, the Group delivered underlying revenue growth of 2% and a 90bps improvement in trading profit margin, in line with guidance. Performance improved over the course of the year, with 1% underlying revenue growth in the first half and 3% in the second half. Highlights included our continued strength in the Emerging Markets, with China delivering double-digit growth. At a franchise level, our Knee Implants franchise continued to deliver market-beating growth and Hip Implants improved markedly in the second half. In Sports Medicine REGENETEN for shoulder repair, acquired in December 2017, had an outstanding year as we more than doubled sales and the acquisition of Ceterix, completed in early 2019, offers exciting opportunities in knee repair. Our performance in

Advanced Wound Care and Advanced Wound Devices in the US also stood out across 2018. The team delivered these successes whilst controlling costs. This contributed to the margin growth, which also included a gain from a one-off legal settlement. Most impressively, the significant change in structure and leadership in the second half did not detract from delivery and the stronger finish to the year.

Pay for performance is important to us and therefore members of the Audit Committee joined us to consider our results and determine the extent to which performance against the targets in our incentive plans were met. Taking into account this financial performance along with consideration of how our Executive Directors performed against their business performance objectives, the Remuneration Committee determined that Namal Nawana would receive a cash incentive payment of 67.7% of his full year's salary and an Equity Incentive award of 35.9% of his full year's salary (prorated to reflect his joining date in May 2018) and that Graham Baker would receive a cash incentive payment of 95.5% of his salary and an Equity Incentive award of 50% of his salary (pro-rated to reflect his increase in salary from July 2018 to reflect increased responsibilities). The Committee also determined that Olivier Bohuon would receive a cash incentive payment of 94% of his salary in respect of the period worked as Chief Executive Officer to May 2018, when he retired from the Board. Reviewing the performance of the Company, the Committee was confident that these outcomes appropriately reflected our underlying performance over the year as a whole.

The Committee also reviewed performance over the past three years and determined that 93% of the target Performance Share Plan awards made in 2016 to Olivier Bohuon would vest reflecting the performance of the Company as a whole. Namal Nawana and Graham Baker were not employed by the Company at the time these awards were made.

The total remuneration paid to Namal Nawana, Olivier Bohuon and Graham Baker in 2018 is detailed further on page 89.

Looking forward – remuneration arrangements for 2019

As explained on pages 8–11, the Board approved a new strategy during 2018 and Namal articulated his vision for the business externally earlier in 2019. During the course of 2019 our focus will be on developing remuneration arrangements to align with this strategy and to drive the performance and behaviours to deliver that strategy. We shall engage with shareholders during the course of 2019 to ensure firstly that shareholders understand our business strategy and secondly how we intend to align our remuneration

arrangements to that strategy. We shall ensure that shareholder views are appropriately reflected in the Remuneration Policy we submit at the 2020 Annual General Meeting.

Looking forward – UK corporate governance code

We are mindful of the corporate governance changes which have come into effect at the beginning of 2019. During 2018, we discussed how we would be addressing these changes. We have updated our Terms of Reference to expand our remit to consider pay and benefits across the Company in more depth and breadth than before. The review of our Remuneration Policy in 2019 will also consider the new provisions of the UK Corporate Governance Code.

Although we are not required to report on the CEO pay ratio until next year, we have compared the pay of our outgoing Chief Executive Officer, Olivier Bohuon and our new Chief Executive Officer, Namal Nawana to the median pay in the UK and determined that our CEO pay ratio is 95:1. Further details are given on page 102.

Appointment of Namal Nawana

We determined the remuneration arrangements for Namal Nawana, our incoming Chief Executive Officer, having regard both to the remuneration policy approved by shareholders in 2017 and also to the competitive market environment for Medical Devices Chief Executives of Namal's calibre and experience, most of whom are based in the US. We are very grateful for the support and guidance we received from the shareholders we spoke to when we were considering appropriate remuneration arrangements.

His remuneration arrangements are described more fully in the following pages. Namal is employed on a standard US executive contract. He receives a base salary of \$1,540,000 and participates in the Annual Incentive Plan (cash and equity) and the Performance Share Plan. He also participates in the retirement plans available to our US Executives: Executive Plus Plan, 401k and 401k plus. The Company contribution to these plans is: 20% of base salary to the Executive Plus Plan, standard company match for 401k and standard 401k plus contribution up to the IRS maximum. He will be required to give six months' notice and the notice period from the Company is 12 months. He received no sign-on or buy-out award on joining the Company.

Executive officer remuneration

We also considered and approved remuneration arrangements for a number of Executive Officers who have moved into new roles or joined the Company as part of Namal's review of the leadership team and organisational structure. In particular, we consulted shareholders over the summer with regard to increasing our Chief Financial Officer, Graham Baker's base salary by 5% to reflect his increased responsibilities for our IT and Global Business Services functions. We are grateful to those shareholders who responded to this consultation and were overwhelmingly supportive. We reached out to the holders of over 40% of our share capital and received responses from nearly half of these shareholders, all of whom were supportive.

Retirement of Olivier Bohuon

We also determined the retirement arrangements for Olivier Bohuon, our former Chief Executive Officer, in line with the Remuneration Policy approved by our shareholders in 2017.

Olivier stepped down from the Board on Namal's appointment in May 2018 and remained employed in an advisory capacity supporting the transition for a period of six months, during which time he continued to receive the same

salary and benefits as in 2017. He participated in the Annual Incentive Plan for the period worked as Chief Executive Officer in 2018, but did not receive a 2018 award under the Performance Share Plan. As a good leaver, his Equity Incentive Awards vested on his retirement date on 7 November 2018, and his Performance Share Awards have been 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 remains subject to a two-year post vesting holding period.

2018 Annual general meeting

We were pleased that our Remuneration Report received over 97% of votes in favour at the 2018 Smith & Nephew plc AGM. This demonstrates the strong support from our shareholders for our remuneration arrangements.

I should like to thank the shareholders who have engaged with us and supported us during the year and particularly those I met as part of my induction programme.

I should also like to thank my fellow Committee members for their support during the year and to welcome Deloitte as our new remuneration advisors.

LOOKING FORWARD

In summary, our focus for 2019 includes:

- > Developing a new Remuneration Policy to align with the new strategy to deliver the performance and behaviours required to deliver the results.
- > Engaging with key shareholders whilst developing a new Remuneration Policy to ensure alignment of views.
- > Continuing to develop our understanding and oversight of pay arrangements across the Group focusing particularly on the CEO pay ratio and the gender pay ratio.

Angie Risley

Chair of the Remuneration Committee

The Terms of Reference of the Remuneration Committee describe the role and responsibilities more fully and can be found on our website at www.smith-nephew.com.

Directors' Remuneration Report
Remuneration Committee report continued

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

Growth (8.3%)	Revenue growth through achieving the full potential of our portfolio transforming our business through enabling technologies and expanding in high growth segments is fundamental to our future success.
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.

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 Free 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.

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 89 to 105) 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 11 April 2019. The Implementation Report explains how the Remuneration Policy was implemented during 2018 and also how it is currently being implemented in 2019.

The second part of the Report (pages 106 to 114) 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 2019 and it is intended that it will next be put to shareholder vote at the Annual General Meeting to be held in 2020.

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 11 April 2019.

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.

WORK OF THE REMUNERATION COMMITTEE IN 2018

In 2018, we held five meetings and determined ten matters by written resolution, mainly relating to Executive Officer Remuneration and termination packages and the appointment of Deloitte LLP as new Remuneration Committee advisors. Each meeting was attended by all members of the Committee. 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, in the first part of the year and Deloitte in the second half of the year without management present. Our programme of work in 2018 can be found in the table on the next page.

Since year end, we have also reviewed the financial results for 2018 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 2019. 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 2016. Finally, we approved the wording of this Directors' Remuneration Report.

INDEPENDENT REMUNERATION COMMITTEE ADVISORS

During the year, the Remuneration Committee received information and advice from both Willis Towers Watson and Deloitte LLP. Both firms are independent executive remuneration consultancy firms appointed by the Remuneration Committee following a full tender process in 2011 and 2018 respectively. Deloitte LLP replaced Willis Towers Watson as our primary Remuneration advisors in July 2018, although Willis Towers Watson continue to provide market benchmark data on compensation design and levels for our Executive Director and Executive Officer positions. During the year, both firms provided advice on market trends and remuneration issues in general, attended Remuneration Committee meetings, assisted in the review of the Directors' Remuneration Report, undertook calculations relating to the TSR performance conditions, advised on Executive Director and Officer pay and investor views and engagement.

The fees paid to Deloitte LLP for Remuneration Committee advice during 2018, charged on a time and expense basis, were £68,200 and the fees paid to Willis Towers Watson were £91,000. Deloitte LLP also provided other tax and consultancy services to the Company. Willis Towers Watson also provided other human resources and compensation advice to the Company for the level below the Board. Both Deloitte LLP and Willis Towers Watson 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.

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Directors' Remuneration Report

	Late January	Early February	July	September	October
	Approval of salaries, awards and payouts in 2018	Approval of targets and Remuneration strategy for 2018	Mid-year Review of Remuneration Arrangements	Review of Graham Baker's base pay	Review of Remuneration Strategy
DETERMINATION OF REMUNERATION POLICY AND PACKAGES					
Determination of Remuneration Policy for Executive Directors and senior executives.	Approved quantum of cash payments and awards to Executive Directors and Officers under the Annual Incentive Plan, the Equity Incentive Programme and Performance Share Programme, (in the context of 2017 financial performance).	Agreed the targets for the short-term and long-term incentive plans for 2018. Approved the remuneration strategy for 2018 against the proposed business plan.	Report from Deloitte on current market trends in remuneration matters and an analysis of how the Company's remuneration arrangements aligned with current practices elsewhere.	Approved 5% base salary increase for Graham Baker to reflect his increased responsibilities for the IT and Global Business Services functions following consultation with the holders of 40% of the Company's shares.	Agreed to update the Company's Remuneration Policy to align with the new corporate strategy during 2019 to put to shareholders for approval in 2020.
Approval of individual remuneration packages for Executive Directors and Executive Officers, at least annually, and any major changes to individual packages throughout the year.	Reviewed the fees for the Chair, Executive Directors and Officers.	Considered appropriate remuneration package for new Chief Executive Officer.	Reviewed the performance of long-term awards granted in 2016, 2017 and 2018.		Agreed to make minor adjustments to certain targets and measures in 2019 in line with the existing remuneration Policy.
		Reviewed Chair's pay.			Reviewed benchmarking data for the Executive Directors and Executive officers prepared in accordance with agreed methodology.
Consideration of remuneration policies and practices across the Group in particular relating to CEO Pay ratio and Gender Pay.					Considered reports on Gender Pay Gap.

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.

Reviewed adherence to shareholding guidelines for Directors and Senior Management.

Monitored dilution limits and the number of shares available for use in respect of Executive and all-employee share plans.

Approved amendments to various share plan rules to reflect regulatory changes.

REPORTING AND ENGAGEMENT WITH SHAREHOLDERS ON REMUNERATION MATTERS

Approval of the Directors' Remuneration Report ensuring compliance

Approved the Remuneration Report.

Reviewed the shareholder response to the Remuneration Report at the AGM and noted feedback.

Reviewed the shareholder response to the Remuneration Report at the AGM and noted feedback.

with related
governance
provisions.

Continuation
of constructive
engagement on
remuneration
matters with
shareholders.

OTHER MATTERS

Audit Committee in
attendance to answer
questions related to
audited numbers and
provide assurance.

Confirmed the
appointment of
Deloitte LLP as the
new independent
advisors to the
Committee.

Discussed
recent corporate
governance changes
and the impact they
would have on the
Remuneration
Committee.

Remuneration implementation report

SINGLE TOTAL FIGURE ON REMUNERATION

The amounts for 2018 have been converted into US\$ for ease of comparability using the exchange rates of £ to US\$1.334 and € to US\$1.180 (2017: £ to US\$1.2877 and € to US\$1.1279).

	Namal Nawana Appointed 7 May 2018		Olivier Bohuon Appointed 1 April 2011 (resigned from Board 7 May 2018)		Graham Baker Appointed 1 March 2017		Julie Brown Appointed 4 February 2013 (resigned with effect from 11 January 2017)	
	2018	2017	2018	2017	2018	2017	2018	2017
FIXED PAY								
Base salary	\$ 1,006,923	–	\$ 490,615	\$ 1,330,347	\$ 707,628	\$ 547,273	–	\$ 21,600
Pension payments	\$ 222,010	–	\$ 147,184	\$ 399,104	\$ 212,302	\$ 164,182	–	\$ 6,482
Taxable benefits	\$ 59,754	–	\$ 44,322	\$ 177,433	\$ 26,758	\$ 22,308	–	\$ 637
ANNUAL VARIABLE PAY								
Annual Incentive Plan – cash	\$ 1,042,655	–	\$ 455,345	\$ 1,208,911	\$ 676,025	\$ 683,797	–	–
HYBRID PAY								
Annual Incentive Plan – equity	\$ 552,290	–	–	\$ 665,173	\$ 353,817	\$ 361,200	–	–
LONG-TERM VARIABLE PAY								
Performance Share Plan	–	–	\$ 1,193,678	\$ 1,335,721	–	–	–	–
Total	\$ 2,883,632		\$ 2,331,144	\$ 5,116,689	\$ 1,976,530	\$ 1,778,760		\$ 28,720

Base salary the actual salary receivable for the year.

Pension payments the value of the salary supplement in lieu of pension or contribution to any pension scheme made by the Company.

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 94–95 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 2019 this is based on an estimated share price of 1,380.98p per share, which was the average price of a share over the last quarter of 2018. The value of the 2015 share awards that vested in 2018 have now been restated with the share price on the date of actual vesting being 1,325.65p per share on 9 March 2018.
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 2018, 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.

Directors' Remuneration Report

Remuneration implementation report continued

FIXED PAY

Base salary

In February 2018, it was agreed that with effect from 1 April 2018, Executive Directors would be paid the following base salaries per annum.

	2018	2017
Olivier Bohuon (retired from Board on 7 May 2018 and from Company on 7 November 2018)	€1,179,490	€1,179,490
Graham Baker	£520,000	£510,000

Namal Nawana was appointed Chief Executive Officer on 7 May 2018 and paid a base salary of \$1,540,000 per annum.

After a period of consultation with shareholders, Graham Baker's salary was increased by 5% to £546,210 to take effect from 1 July 2018, when he assumed additional responsibilities for the IT and Global Business Services functions.

In February 2019, 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 2.9% in the UK and 3% in the US. The Remuneration Committee has agreed that Namal Nawana's salary will increase by 2.5% and Graham Baker's salary will increase by 2% to \$1,578,500 and £557,134 respectively with effect from 1 April 2019.

Pension Payments

In 2018, Graham Baker and Olivier Bohuon, until his retirement from the Company on 7 November 2018, 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.

Namal Nawana participates in the retirement plans available to our US Executives: Executive Plus Plan, 401k and 401k plus. During 2018, total Company Pension and 401k contributions for Mr Nawana amounted to \$222,010 which on an annualised basis is equivalent to 21.34% of salary. Due to the fact that Mr Nawana reached the annual cap on 401k contributions in the period from joining on 7 May 2018, the actual percentage for 2018 equated to 22.05%. For 2019, the combined pension and 401k Company contribution is expected to be less than 21.47% of his base salary.

Benefits

In 2018, our UK based Executive Directors (Olivier Bohuon and Graham Baker) 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. Namal Nawana participated in the US Life Assurance Program, which in total is

capped at \$2 million. 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 2019 for Namal Nawana and for Graham Baker. The following table summarises the value of benefits in respect of 2017 and 2018. Olivier Bohuon and Julie Brown received these benefits until they retired from the Board on 7 May 2018 and 11 January 2017 respectively.

	Namal Nawana		Olivier Bohuon		Graham Baker		Julie Brown	
	2018	2017	2018	2017	2018	2017	2018	2017
	\$	–	£2,915		£1,369			
Health cover	6,635			£17,807		£1,217	–	£44
	\$	–	£5,288		£17,676			
Car and fuel allowance	8,467			£15,000		£14,182	–	£451
Financial consultancy advice	£33,485	–	£15,733	£34,204	£1,020	£1,925	–	–
	–	–	–	€37,736	–	–	–	–
Travel costs	–	–	£7,056	£33,703	–	–	–	–
Subscriptions	–	–	£2,245	£4,023	–	–	–	–

ANNUAL VARIABLE PAY

Annual Incentive Plan 2018 – cash element

The performance measures and weightings which apply to the cash element of the Annual Incentive Plan are set out in the Remuneration Policy approved by shareholders in 2017 and detailed on page 108.

The weightings of the performance measures and the figures for threshold, target and maximum relating to the financial objectives of the cash element can be summarised as follows:

	Weighting	Threshold	Target	Maximum	Actual
Revenue	35%	\$4,887m	\$5,039m	\$5,190m	\$4,960m ¹
Trading profit margin	25%	22.0%	22.5%	22.9%	22.7%
Trading cash flow	15%	\$886m	\$985m	\$1,083m	\$951m

¹ At constant exchange rates. See page 131.

The Committee determined that this performance fairly reflected the overall performance of the Company during 2018 and therefore resulted in a bonus achievement of 71% of salary in respect of the financial objectives.

	Weight	Achieved % of target	Award % of salary
Revenue	35	74	25.9
Trading profit margin	25	129	32.3
Trading cash flow	15	83	12.5

Accordingly, the following amounts have been earned by Namal Nawana and Graham Baker under the cash element of the Annual Incentive Plan in respect of their financial objectives.

Namal Nawana (pro-rated to reflect date of joining Company 7 May 2018)	\$	708,268
Graham Baker (pro-rated to reflect change to salary from 1 July 2018)	£	374,287

The same measures and weightings will apply to the financial measurements of the cash element of the Annual Incentive Plan 2019. For reasons of commercial sensitivity, we are unable to disclose the precise targets now, but they will be disclosed in full in the 2019 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.

The table on page 92 overleaf sets out how Namal Nawana and Graham Baker have performed against the business objectives of People, Business Process and Customers.

Directors' Remuneration Report

Remuneration implementation report continued

Namal Nawana

People

– Assessed and took action at the senior leadership level designing a new operating model and attracting four new Executive Committee leaders to Smith & Nephew as well as numerous vice presidents. Improved diversity and aligned team in support of the new purpose, culture pillars and strategic imperatives.

– Successfully launched new brand purpose – Life Unlimited – culture pillars and winning behaviours. Engaged organisation with more than 40% of employees actively participating in the process.

– Implemented an employee engagement platform through the introduction of Company-wide live, interactive broadcast meetings and extended face-to-face engagement opportunities with >20% of global employee base through face-to-face Town Halls, factory and other site meetings.

Business Process

– Completed a robust market and internal organisational assessment as well as external benchmarking to inform the development of a clear strategy resulting in a newly designed operating model including a flatter, franchise-led organisational design with global supporting functions.

– Introduced new Company strategy with five imperatives to drive medium and long-term value creation for shareholders with detailed and robust KPIs put in place internally for continuous measurement throughout the relevant period.

– Engaged with R&D organisations in all business areas and reprioritised programmes to align with strategy. Personally led robotic

Graham Baker

– Key accomplishments in 2018 included strengthening Finance leadership team and improving diversity, as well as successfully integrating Global Business Services and IT following transfer of additional responsibilities mid-year. Supported successful CEO transition including assessment of the overall Company and design of the new organisational operating model.

– Strong delivery of APEX restructuring programme, at both Group level, with around \$60 million of benefits realised and tight control of operating expenditure, and in Finance function with successful insourcing of transaction processing and IT upgrades. Delivered a significantly improved full year trading margin and built robust plans for further multi-year expansion. Additionally, delivered meaningful reduction in trading tax rate¹ for 2018, down to 16.1%.

programme acceleration and the team exceeded overall target of 80% key product launches delivered to plan.

Customers

- Demonstrated strong customer focus meeting with hundreds of customers in aggregate including through hospital visits and attending medical education events and industry conferences.
- Engaged regularly with key shareholders and investors through face-to-face meetings built around the financial calendar and key investor conferences in London and the United States.
- Delivered significant shareholder returns through strong stock out-performance of FTSE 100 index and improved dividend distribution.

– Regular engagement with shareholders, supporting financial calendar reporting and key investor conferences, as well as management of debt provider and other key financial stakeholders. Delivered significant shareholder returns through strong stock out-performance of FTSE 100 index and improved dividend distribution.

This resulted in a bonus achievement of 33.2% of salary in respect of the business objectives.

	Weight	Achieved % of target	Award % of salary
People	8.33%	133%	11.1%
Business Process	8.33%	116%	9.7%
Customers	8.33%	150%	12.5%

Accordingly, the following amount has been earned by Namal Nawana under the cash element of the Annual Incentive Plan in respect of his business objectives.

Namal Nawana (pro-rated to reflect date of joining Company 7 May 2018) \$
334,387

This resulted in a bonus achievement of 25% of salary in respect of the business objectives.

	Weight	Achieved % of target	Award % of salary
People	8.33%	100%	8.33%
Business Process	8.33%	100%	8.33%
Customers	8.33%	100%	8.33%

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 (pro-rated to reflect 5% salary increase with effect from 1 July 2018) £132,664

As well as considering the monetary outcome of the formulaic calculation of these awards, the Committee considered whether discretion should be applied to override these formulaic outcomes and concluded that the monetary outcomes were aligned with the financial performance of the Company, individual performance during 2018 and the intention of the Remuneration Policy.

For 2019, the business objectives for the Executive Directors will be; Growth, People, and Business Processes to align with the new Strategic Imperatives. These business objectives will be equally weighted.

The Committee also considered the level of Cash Incentive Payment to be made to Olivier Bohuon who retired as Chief Executive Officer on 7 May 2018. 75% of his Cash Incentive Payment was based on the Financial Objectives, which resulted in a payout of 94% of target as described on page 91. 25% of his Cash Incentive Payment was based on his performance against his Business Objectives: People, Business Process and Customers. In 2018, these objectives were all aligned to ensuring an orderly transition to the new Chief Executive Officer. The Committee considered his performance as Chief Executive Officer against these business objectives for the period up to 7 May 2018 and concluded that he had broadly met these objectives and that therefore the payout in respect of his Business Objectives should be in line with the payout in respect of the overall financial objectives at 94% as follows:

	Award %
	Amount of target
Financial Objectives (75% of award)	€289,46394
Business Objectives (25% of award)	€96,488 94
Total Cash Incentive Payment	€385,951

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

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Directors' Remuneration Report

Remuneration implementation report continued

Annual Incentive Plan – equity element

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 what has been achieved	Assessment of how Executive Directors have achieved	Below expectations		
		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 Namal Nawana 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) Namal Nawana 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 Namal Nawana has exceeded expectations and Graham Baker has performed in line with expectations. These ratings result in an Equity Incentive Award of 55% of salary (pro-rated to 35.9% to reflect his appointment on 7 May 2018) for Namal Nawana and 50% of salary for Graham Baker. In summary, as a result of the financial performance described on page 91 and the individual performance described in the table on page 92, the Remuneration Committee determined that the following awards be made under the Annual Incentive Plan in respect of performance in 2018:

Executive Director	Cash Component		Equity Component	
	% of salary	Amount	% of salary	Amount
Namal Nawana	67.7%	\$ 1,042,655	35.9%	\$ 552,290
Graham Baker	95.5%	£506,951	50.0%	£265,328

These figures are converted into dollars and included under Annual Incentive Plan (cash) and (equity) in the single figure table on page 89.

The precise awards granted in 2019 to Namal Nawana and Graham Baker in respect of service in 2018 will be announced when the awards are made and will be disclosed in the 2019 Annual Report. The Committee also determined that no Equity Incentive Award would be made to Olivier Bohuon who had retired as Chief Executive

Officer during the year. As a result of the 2018 performance assessment for Graham Baker, the first tranche of the Equity Incentive Award made in 2018 will vest. Both the grant and vesting of these awards are subject to Graham's performance discussed on page 92. Namal Nawana was not employed during 2017 and therefore received no Equity Incentive award in 2018.

Director	Date of Grant	Number of shares under award	Number of shares to vest from each grant subject to performance
Graham Baker	7 March 2018	7,242	14,485

EQUITY INCENTIVE AWARD FROM PRIOR YEARS

The following Equity Incentive awards held by Olivier Bohuon vested in their entirety on his retirement from the Company on 7 November 2018 in accordance with the plan rules:

Director	Date of Grant	Number of shares under award vested on 7 November 2018
Olivier Bohuon	7 March 2018	41,587
	7 March 2017	28,787
	7 March 2016	17,608

EQUITY INCENTIVE AWARDS IN 2019

The Equity Incentive Award element will operate in 2019 in exactly the same way as in 2018 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 above.

LONG-TERM VARIABLE PAY

Performance Share Plan

Performance Share Programme – 2018 grants

Performance share awards granted in 2018 were made to Graham Baker and to Namal Nawana on his appointment under the Global Share Plan 2010 to a maximum value of 190% of salary (95% for target performance). As Olivier Bohuon had already indicated his intention to retire at the time the awards were made in 2018, no award was made to him. 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 2018 and awards will vest subject to performance and continued employment in 2021. 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 groups is independently monitored and reported to the Remuneration Committee by Deloitte LLP.

Total Shareholder Return (TSR) performance is relative to two separate indices as follows:

Relative TSR ranking	Award vesting as % of salary at date of grant	
	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 against both indices, none of this part of the award will vest.

Directors' Remuneration Report

Remuneration implementation report continued

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:

$$\frac{\text{Net Operating Profit}^1 \text{ less Adjusted Taxes}^2}{(\text{Opening Net Operating Assets} + \text{Closing Net Operating Assets})^3} \div 2$$

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, borrowings 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 11.6%	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 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 2018	Award vesting as % of salary
Below Threshold	Nil

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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 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 \$1,575m	Nil
\$1,575m (13% of target)	11.875%
\$1,810m	23.75%
\$2,046m or more (+13% of target)	47.5%

Performance Share Programme 2019

Performance share awards will be made in 2019 to the Executive Directors under the Global Share Plan 2010 to a maximum value of 190% of salary (95% for target performance). Performance will be measured over the three financial years commencing 1 January 2019 against the same four equally weighted performance measures as in 2018: 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 the Executive Directors 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 2018 as described on page 95 against the same two peer groups.

Return on invested capital (ROIC) will be measured in the same way as in 2018, as described on page 96.

The targets will be as follows:

Return on Invested Capital	Award vesting as % of salary
Below Threshold 11.8%	Nil
Threshold 11.8% (1.25% of target)	11.875%
Target 13.1% (as derived from the Strategic Plan)	23.75%
Maximum or above 14.3% (+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 2018, as described on page 96. The targets will be as follows:

Sales growth over three-year period commencing 1 January 2019	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 2021 Annual Report, when the Committee will discuss performance against the target.

Cumulative free cash flow will be measured in the same way as in 2018, as described on page 96. The targets will be as follows:

Cumulative free cash flow	Award vesting as % of salary
Below \$1,923m	Nil
\$1,923m (13% of target)	11.875%

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\$2,210m	23.75%
\$2,497m or more (+13% of target)	47.5%

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Directors' Remuneration Report

Remuneration implementation report continued

Performance Share Programme 2016

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 2016. Vesting of the conditional awards made in 2016 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 2016.

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 2016 was \$2,316 million with a target of \$2,725 million. Over the three-year period, the adjusted revenues in Emerging Markets were \$2,560 million. These adjustments include translational foreign exchange. This part of the award therefore vested at 20% 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 \$1,929 million which is between target and maximum. These adjustments include items such as Board-approved M&A, including the acquisition of Rotation Medical and the disposal of the Gynaecological business and Board-approved Business Plans such as the APEX programme, the commercial restructuring programme and exceptional expenditure to comply with the EU Medical Devices Regulations. This part of the award therefore vested at 73%.

	Threshold	Target	Maximum	Actual	Percentage
TSR	Median	–	Upper Quartile	Below Median	0%
Emerging Markets Sales	\$2,316m	\$2,725m	\$3,133m	\$2,560m	20%
Cumulative Free Cash Flow	\$1,585m	\$1,822m	\$2,059m	\$1,929m	73%

Overall therefore, the conditional awards made in 2016 will vest at 93% of target (46.5% of maximum) on 7 March 2019 as follows:

Director	Date of grant	Number of shares under award at maximum	Number vesting
Olivier Bohuon	7 March 2016	139,396	64,819

Pro-rated for length of time held prior to retirement from the Company on 7 November 2018

As well as considering the monetary outcome of the formulaic calculation of these awards, the Committee considered whether discretion should be applied to override these formulaic outcomes and concluded that the monetary outcomes were aligned with the financial performance of the Company during the performance period and the intention of the Remuneration Policy.

Neither Namal Nawana nor Graham Baker were employed by the Company in 2016 and therefore have no Performance Share Awards to vest on 7 March 2019.

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 page 95–97.

		Number of ordinary shares	
	Date granted	under award at maximum	Date of vesting
Olivier Bohuon	7 March 2016	139,396 ^{1,2}	7 March 2019
	7 March 2017	97,744 ^{1,2}	7 March 2020
Graham Baker	7 March 2017	79,166	7 March 2020
	7 March 2018	75,058	9 March 2021
Namal Nawana	9 May 2018	108,800	9 May 2021

1 Pro-rated to reflect Olivier Bohuon’s retirement from the Company on 7 November 2018.

2 On 5 February 2019, 53.5% 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

	Namal Nawana ¹		Olivier Bohuon ²		Graham Baker ¹	
	Number of shares	Face value	Number of shares	Face value	Number of shares	Face value
Annual Equity Incentive Award (see page 94)	–	–	40,801	€589,745	21,727	£280,500
Performance Share Award at maximum (see page 98)	108,800	£1,419,311	–	–	75,058	£969,000

1 Annual Equity Incentive Awards for 2018 were based on performance for 2017, hence Namal Nawana received no award.

2 Olivier Bohuon did not receive a Performance Share Award in 2018, as he had announced his intention to retire.

Please see Policy Table on pages 108 and 109 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 2018 was 1291p, and for the awards granted on 9 May 2018 was 1304.5p.

SINGLE TOTAL FIGURE ON REMUNERATION

Chair and Non-Executive Directors

Director	Basic annual fee ¹		Committee Chairman /Senior Independent Director fee		Intercontinental travel fee		Total	
	2018	2017	2018	2017	2018	2017	2018	2017
Roberto Quarta	£ 418,695	£ 412,000	–	–	–	£		