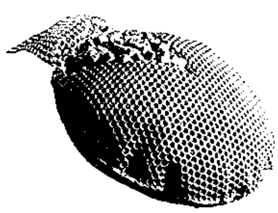
324357

Contents

Smith & Nephew is a leading worldwide healthcare group operating in major growth markets, concentrated in the areas of wound management, orthopaedics and consumer healthcare.

Front Cover and Below
Allevyn Cavity hydrocellular deep wound dressings have a three dimensional honeycombed outer surface for effective non-adherency and a core of highly absorbent foam chips



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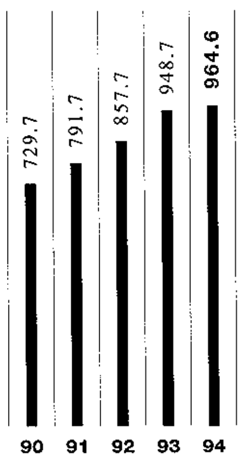
COMPANIES HOUSE 19/05/95

financial highlights

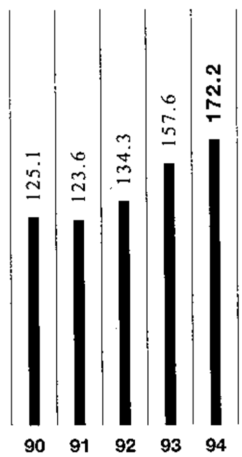
Another year of strong organic growth with the Group outperforming its markets, enabling dividends to increase by 8%

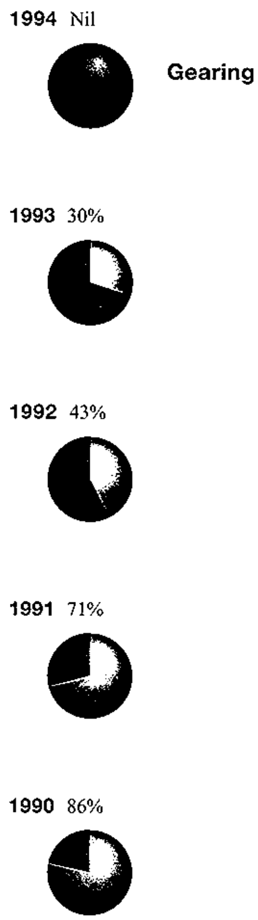
At 31 December 1994	**1994** *£ million*	1993 *£ million*	*% change*
Turnover	964.6	948.7	+2%
(Loss)/Profit before taxation			
before exceptional items	172.2	157.6	+9%
after exceptional items	(5.5)	164.9	
Adjusted earnings per share	10.62p	10.15p	+5%
(Loss)/Earnings per share	(4.96p)	10.55p	
Dividends per share	5.28p	4.91p	+8%

Turnover *£ million*

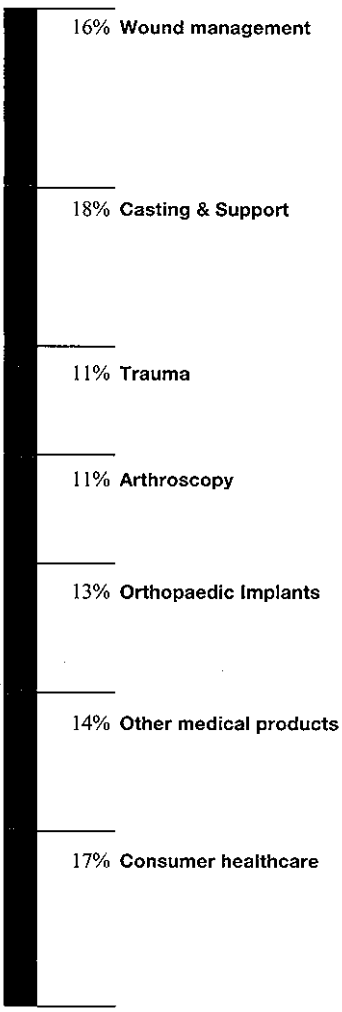


Profit before tax & exceptional items *£ million*



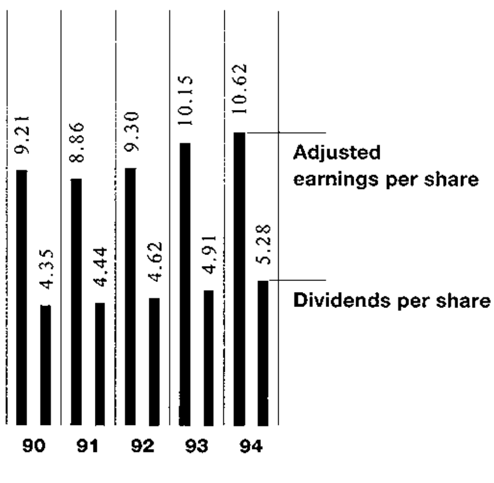


Product Groups



1994 Sales from Continuing Operations

Over recent years, Smith & Nephew has substantially strengthened its finances and established strong organic growth from a core range of innovative products



chairman's statement

Smith & Nephew can now take advantage of opportunities to enhance growth on the foundations of a strong balance sheet, organisation and product range

The Group achieved another year of consistent progress with underlying sales growth of 7%. The second half of the year reflected an improving performance and strong growth in our main product areas again led to increases in market shares.

Pre-tax profits before exceptional items have increased 9% and operating profit margins before exceptional items have increased from 17.9 % in 1993 to 18.2 %.

During the year we disposed of our intraocular lens operation, Ioptex. It had started to lose money and the market was not recovering from the significant erosion in prices caused by a reduction in Medicare insurance reimbursement which began in the early 1990's. A certain amount of restructuring of the industry had already taken place and we took the opportunity to dispose of the operation to Allergan Inc, a major eye care company. An exceptional loss of £150m was made on the disposal, of which £141m related to goodwill, previously written off at the time of the original acquisition and £9m related to net assets at the date of sale.

In addition, the Group has charged £27m against profits to cover a programme of cost reduction and rationalisation of certain manufacturing facilities and for a restructuring of distribution across Continental Europe. The cash cost of this will be £23m spread over 1995 and 1996.

The Board is recommending a final dividend of 3.26p per ordinary share which represents an increase of 8% on the final dividend last year. Together with the interim dividend of 2.02p per share paid on 12 December 1994, this amounts to a total for the year of 5.28p, an increase of 8%.

During the early part of the 1980's Smith & Nephew underwent a period of concentration on organic development with emphasis on cost reduction. This laid the foundations for a period of intense acquisition activity in the second half of the decade. There followed a further period of consolidation during the first half of the 90's with concentration again on internal growth and cash generation. We can now take advantage of opportunities to enhance growth on the foundations of a strong balance sheet, organisation and product range.

As a leading global healthcare group, our strategy is to consolidate and strengthen the Smith & Nephew Group as a major influence in key markets. We continue to search for acquisitions which will complement and contribute to organic growth. By concentrating on specialist market areas with global growth potential, we will maintain a position in the top rank of healthcare companies.

There has been no change to the membership of your board. It is well balanced between executive and non-executive directors. The varied skills and expertise of our non-executive directors make a very positive and wide ranging contribution to the development of the Group. Each member of the board is committed to maintaining our long established high standards of corporate governance.

As mentioned in my statement last year, we have an organisation in place to pursue positively environmental improvements throughout the Group. Each Smith & Nephew division around the world considers itself part of the local environment and is sensitive to behaving as a good community member. We also ensure that there is a clear understanding by every employee regarding the ethical standards to which we are committed. There is an additional description on each of these areas in the Directors' Report on pages 31 and 32.

The Smith & Nephew Foundation maintains its reputation for significant contribution to medical training and research. Further details of this can be found in the Directors' Report on page 32.

We do not anticipate any major changes in market conditions in 1995. However, Smith & Nephew consistently demonstrates its ability to grow in challenging circumstances and we expect the strength of our innovation and technology will further sharpen our competitive edge.

We will continue to invest strongly in our research and development, our manufacturing base, and our sales and marketing organisations whilst actively pursuing opportunities for acquisition.

Eric Kinder

ERIC KINDER
Chairman

Smith & Nephew board

ALAN FRYER 53
Group Director – UK and Europe
He joined the Group in 1969 and was appointed a Director in 1987. Also a non-executive Director of Hunting plc.

ALASTAIR MACPHERSON 50
Non-executive Director
A non-executive Director since 1986. Chairman of the Audit Committee. A partner at Ashurst Morris Crisp. Also a non-executive Director of Thomas Jourdan plc.

JOHN ROBINSON 54
Chief Executive
He joined the Group in 1979 and was appointed a Director in 1981. Also a non-executive Director of Delta plc.

KENNETH KEMP
Honorary Life President

MICHAEL PARSON
Secretary

Members of the Remuneration Commitee
Members of the Audit Commitee

SIR ANTHONY CLEAVER 56
Non-executive Director
Appointed a non-executive Director in March 1993. He is Chairman of the UK Atomic Energy Authority, General Cable plc, and Business in the Environment. Also a non-executive Director of General Accident plc and Loral Aerospace Systems Integration Corporation.

DR NANCY LANE 58
Non-executive Director
A non-executive Director since 1991. Dr Lane chairs the Group's Scientific Advisory Panel. She is an Official Fellow at Girton College, a Cell Biologist at Cambridge University, and works with the Cabinet's Development Unit on Women in Science, Engineering and Technology.

JACK BLAIR 52

Group Director – North America and Japan

He joined Richards Manufacturing Company in 1980 which was acquired by the Group in 1986. He was appointed a Director in 1989. Also a Director of National Commerce Bancorporation, USA.

SIR FRANCIS KENNEDY 68

Non-executive Director

A non-executive Director since 1988. Chairman of the Remuneration Committee. Also a Director of British Airways plc.

CHRISTOPHER O'DONNELL 48

Group Director – Medical Division

He joined the Group in 1988 and was appointed a Director in 1992.

ERIC KINDER 67

Chairman

He joined the Group in 1957 and was appointed a Director in 1973. Also Chairman of Brunner-Mond Holdings Ltd, a non-executive Director of The Christie Hospital NHS Trust, and Intermediate Capital Group plc.

PETER HOOLEY 48

Group Finance Director

He joined the Group and was appointed a director in 1991.

SIR BRIAN PEARSE 61

Non-executive Director

Appointed non-executive Director in March 1993. Chairman of Lucas Industries plc, The Housing Corporation and British Invisibles. He is Treasurer of King's College, London, Chairman of Young Enterprise and a member of the British Overseas Trade Board.

chief executive's review

The Group is gaining market share in most countries, driving costs down in our manufacturing units to ensure international competitiveness. The innovative strength of our product lines is giving us increasing confidence for the future

During 1994, the Group out-performed the competition in most of the key product sectors, and was able to demonstrate that in our main markets, we are competing strongly with the largest healthcare companies in the world. The five year contract with American Healthcare Systems (AmHS), which should lead to sales of around $400 million, over 5 years, was the most obvious example. We have also been able to satisfy our customers' requirements for cost effective products, whilst more than maintaining margins.

Group Strategy Our strategy is two-fold:

- To ensure our products in all our key sectors are differentiated from their competition by their clinical and cost effectiveness.
- To sell our products worldwide through our highly professional sales and marketing teams.

This strategy is clearly effective as new products launched in the last five years account for one third of healthcare sales.

Underlying sales growth has been particularly encouraging in some key product sectors, for example: Wound Management 11%, Casting 10%, Bandaging 16%, Post Surgical Bracing 12%, and Trauma 8%. This is compared to the low growth affecting the international healthcare industry.

However good our products, they will only gain increasing acceptance with excellent sales and marketing within every major international market.

We have also taken steps to ensure our market leading position by:

- Establishing one UK business for sales to hospitals and primary care. This will focus our selling skills for all product ranges on individual customers, through what is now the largest, single healthcare sales and marketing organisation in the UK.
- Consolidating our sales and marketing in France into one business and also in Germany, by acquiring the majority holding of our German partner BSN.
- Further strengthening sales co-ordination in the USA, particularly in the National Accounts Group resulting in the success in gaining the AmHS contract.

These steps have resulted in real business benefits. We are gaining market share in most countries and the strength of our product lines is giving us increasing confidence for the future. Furthermore, we are driving costs down in our manufacturing units to ensure international competitiveness.

Our balance sheet is now stronger than for many years, with a positive cash balance. As customer buying patterns change, we believe that there will be more scope for reorganisation and acquisition amongst healthcare suppliers. We are in a strong position to take advantage of these changes.

Investment Initiatives As well as ensuring year on year growth, we also invest in the business for long term strength, in particular – business systems, capital projects, research and development and new markets.

As a leading worldwide company, with global products, it is vital that our business systems enable us to manage our products internationally. We are placing considerable emphasis on appropriate information systems, in order to see the true results of our efforts.

Capital investment continues to run at 6% of sales. The major announcement in 1994 was the beginning of a £41m investment over five years for the redevelopment of our Hull site. 'Project Neptune', named after the road where the factory originally started, will ensure our pre-eminent world position in wound management, casting and bandaging products and all anticipated legislative requirements are met well into the next century.

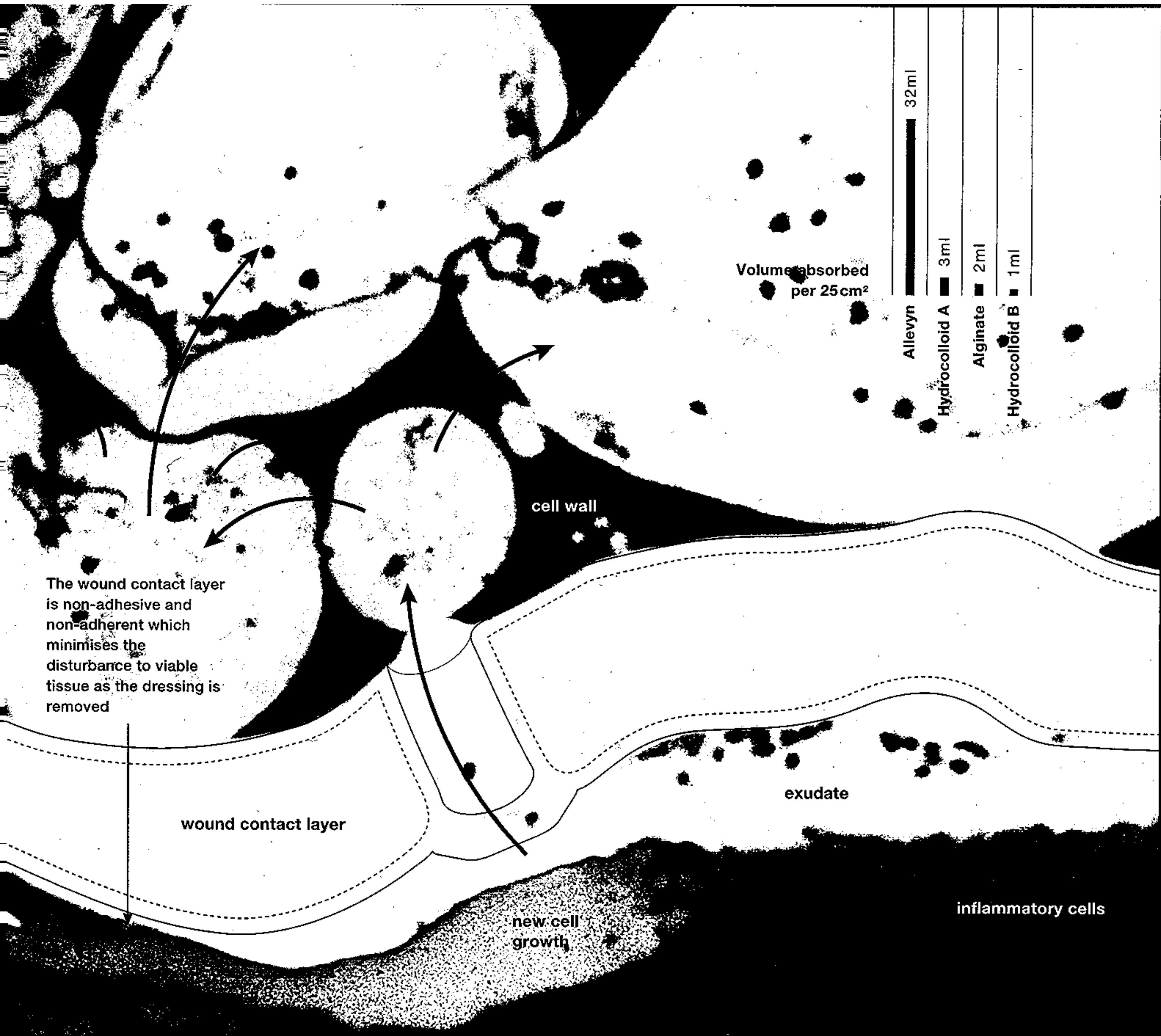
In research and development, we have initiated a number of long-term measures to help to under-pin the long term growth of the Group. The new joint-venture with Advanced Tissue Sciences should enable us to have an innovative cartilage replacement product from tissue engineering by 1999, opening up a whole new business sector for the Group. Our sponsorship of the Smith & Nephew Chair in Biomedical Systems Engineering at Imperial College, London should keep us in the forefront of visualisation technology in arthroscopy and minimally invasive surgery. Other external work in cell-culture and growth factors aimed at orthopaedic applications (particularly those with the Interdisciplinary Research Centre in Biomedical Materials based at Queen Mary and Westfield College London, and with Johns Hopkins University Baltimore), have even longer term significance. The decision to fund a Chair and new research unit in Cellular and Molecular Biology of Tissue Repair at the University of York will provide the understanding to develop new approaches to the repair of damaged tissue.

We continue to invest in potential new markets. Following our success in Japan (33% growth in 1994), we are starting to develop the huge opportunities in China and India. Our new office is now open in China. We are recruiting sales people and investigating potential joint ventures. Our stand-alone medical business in India is now fully operational.

Smith & Nephew People I am very proud of the achievements of our people in many disciplines across the world. I thank everyone for their efforts and successes in 1994. The year has also been a time of considerable change in our human resources programmes. A major effort has gone into methods of identifying and developing skills of the highest order, and I am convinced that both Smith & Nephew people and the Group will benefit enormously from these initiatives.

JOHN ROBINSON
Chief Executive


hydrophilic core
Allevyn is capable of absorbing and retaining large volumes of fluid, even under pressure
new epithelium
dermis
hair follicle
0.01 millimetre



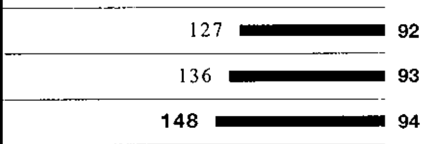
Allevyn deep wound dressings heal faster with fewer dressing changes yielding a

27% cost reduction

per patient healed

The increasing innovative strength of the Group's chronic wound management range is driving sales growth and market share forward across the world

wound management



Sales
of continuing operations
£ million

Geographical analysis of turnover for 1994

A 53% Europe
B 22% America
C 25% Africa, Asia & Australasia

Smith & Nephew wound management sales continued to grow strongly, with an 11% increase on last year. The market has grown by 5%. This excellent performance has moved the Group into No 3 position in the world.

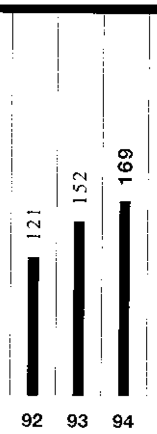
The chronic woundcare market remains the fastest growing sector where Smith & Nephew is growing at 28%, fuelled by particularly good performances in the USA, Europe, Japan, South Africa, Canada and Australia. The Group's success is due to the development and worldwide marketing of technologically-advanced products, such as Allevyn hydrocellular dressings and IntraSite Gel. 1994 saw success for Allevyn on national reimbursement lists, notably the UK, allowing for wider community access to the product and for IntraSite Gel, with a new award-winning pack providing easy directable dispensing.

Profore, a new four layer bandaging system for treating leg ulcers developed in the UK with very strong clinical endorsement, was launched in several international markets, notably the USA. It provides significantly higher healing rates for leg ulcers than traditional bandaging methods.

Cica-Care was launched, a silicone gel treatment for hypertrophic and keloid scarring which is the unsightly discolouration and raising of the join in the skin and surrounding area. The brand achieved a 50% share in this new and rapidly expanding market.

The launch of OpSite Post-Op was also successful bringing for the first time all the advantages of OpSite film, with comfort, conformability and waterproof properties, to the absorbent post operative dressing market. Market share is now being gained from traditional non-woven competitors.

Smith & Nephew continues to play a leading role in the development of woundcare. At the Group Research Centre in York, work on novel materials and adhesives, and on cell-culture approaches have exciting implications for the future of wound healing in general and burns treatment in particular. Adding to the impact of existing external collaborations in the background science at Manchester University and at Guys/St. Thomas' Hospital, sponsorship of the new Smith & Nephew Chair in Tissue Repair at York University should contribute considerably to further successful developments.



Sales
of continuing operations
£ million

Geographical analysis of turnover for 1994

A 41% Europe
B 41% America
C 18% Africa, Asia & Australasia

casting and support

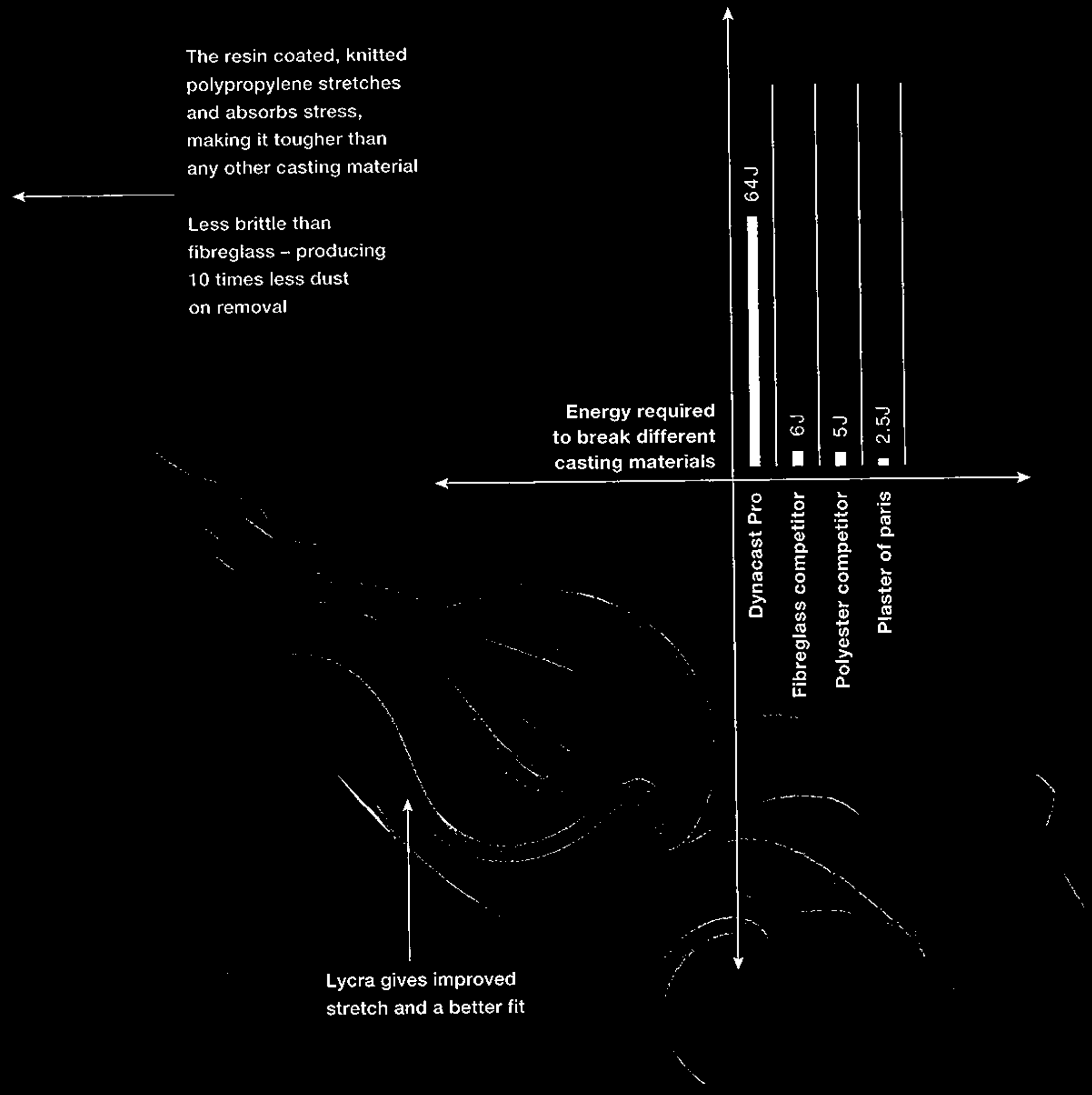
Smith & Nephew sales grew strongly across all product groups in this sector, confirming the Group's leading world market position

Casting sales grew by 10% in a static market which further strengthened the Group's No 2 position. The slow-down in the conversion of the market from plaster of Paris to synthetic casts enabled the Group to further improve its position and increase sales as worldwide leader in plaster of Paris. Plaster of Paris remains an extremely cost effective casting material. Also, growth has continued in our Dynacast range with Dynacast Pro sales increasing by 55%.

As the world's No 1 in bandaging, Smith & Nephew produces the most sophisticated product range available. An outstanding 16% growth was achieved in 1994. In addition to its well established range of adhesive bandages, Smith & Nephew is strongly represented in the advanced cohesive sector with products such as Tensoplus, Easifix and Co-Plus which all grew strongly during the year. The acquisition of the leading UK producer of crepe bandages, Grout and Company, in July 1994, increases the Group's technological capabilities in this sector and brings crepe bandage manufacture and finishing into the Group. This gives new product opportunities in the UK and internationally.

Smith & Nephew is world leader in functional bracing with 43% of the global market and achieved 12% growth in 1994. The Defiance custom brace launched in 1992 is the Group's leading bracing product, with a 19% sales increase. The company successfully entered a new sector of the bracing market in 1994 with the launch of the Monarch osteoarthritis brace. This product was designed to release pressure in the area of the knee affected by the disease, thereby reducing pain for the patient and the need for surgery.

Rehabilitation markets worldwide are growing rapidly, supported by the increasing trend towards clinics and home-care. Smith & Nephew holds a 20% share of its sector and grew by 20% in 1994. The acquisition of Homecraft in February 1995 brings strong representation in Aids for Daily Living, a fast growing sector of the rehabilitation market.



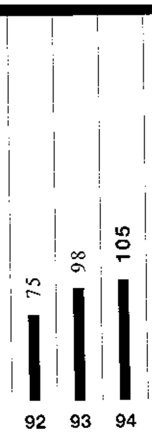
1 millimetre

Dynacast Pro is translucent to X-rays which means routine examinations can proceed without removal of the cast

Dynacast Pro casting material achieved

55% sales growth

by being more comfortable, conformable, easier to apply, tougher and more cost effective



Sales
of continuing operations
£ million

trauma

Strong international sales growth in Europe and Japan underpinned Smith & Nephew's No 2 world market position

Geographical analysis of turnover for 1994

A 17% Europe
B 66% America
C 17% Africa, Asia & Australasia

While the worldwide trauma market increased an estimated 4% in 1994, Smith & Nephew outpaced the global market with underlying sales growth of 8%. The Group holds the No 2 position with a 17% share of the worldwide trauma market.

Trauma is the term for a physical wound or injury caused by a fracture or a blow. Smith & Nephew trauma products include pins, plates, nails and external fixators which help mend serious fractures of the bone.

The Russell-Taylor intramedullary nail system continues to be a key factor in Smith & Nephew's success. A well established product worldwide, new time-saving product additions such as the Orthotrac Coaxial Laser Targeting Device have made surgical procedures easier to perform, providing increased market penetration for Russell-Taylor. It is refinements like these which keep Smith & Nephew at the forefront of trauma development.

In addition to Russell-Taylor, a number of new product lines have added to the success experienced by the Group. The original Ilizarov System, developed for limb-lengthening and to correct bone deformities, was strengthened by the introduction of Acute Trauma Ilizarov, a complete range of new products which make the devices easier to use in trauma applications.

Smith & Nephew formed a spine division, in 1992, which has concentrated on markets such as Japan, the Pacific Rim, South Africa, and Europe for future sales growth. The Simmons Plating and Rogozinski Spinal Rod Systems continue to lead spinal implant sales. Smith & Nephew is leading the spine implant market in the development of minimally invasive surgery through the Kambin Arthroscopic MicroDiscectomy technique. In addition, SecureStrand, a braided polyethylene cable, was introduced in 1994 to fill a niche market for cervical spinal fusion, patella and shoulder fractures.

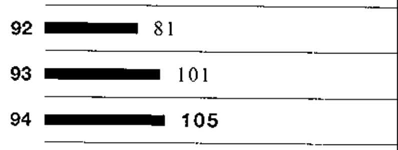
Europe 15% A
America 75% B
Africa, Asia & Australasia 10% C

Geographical analysis of turnover for 1994

Leadership in the arthroscopy market is strengthened by the continued excellence of product range together with world class service and support

arthroscopy

Sales *of continuing operations £ million*

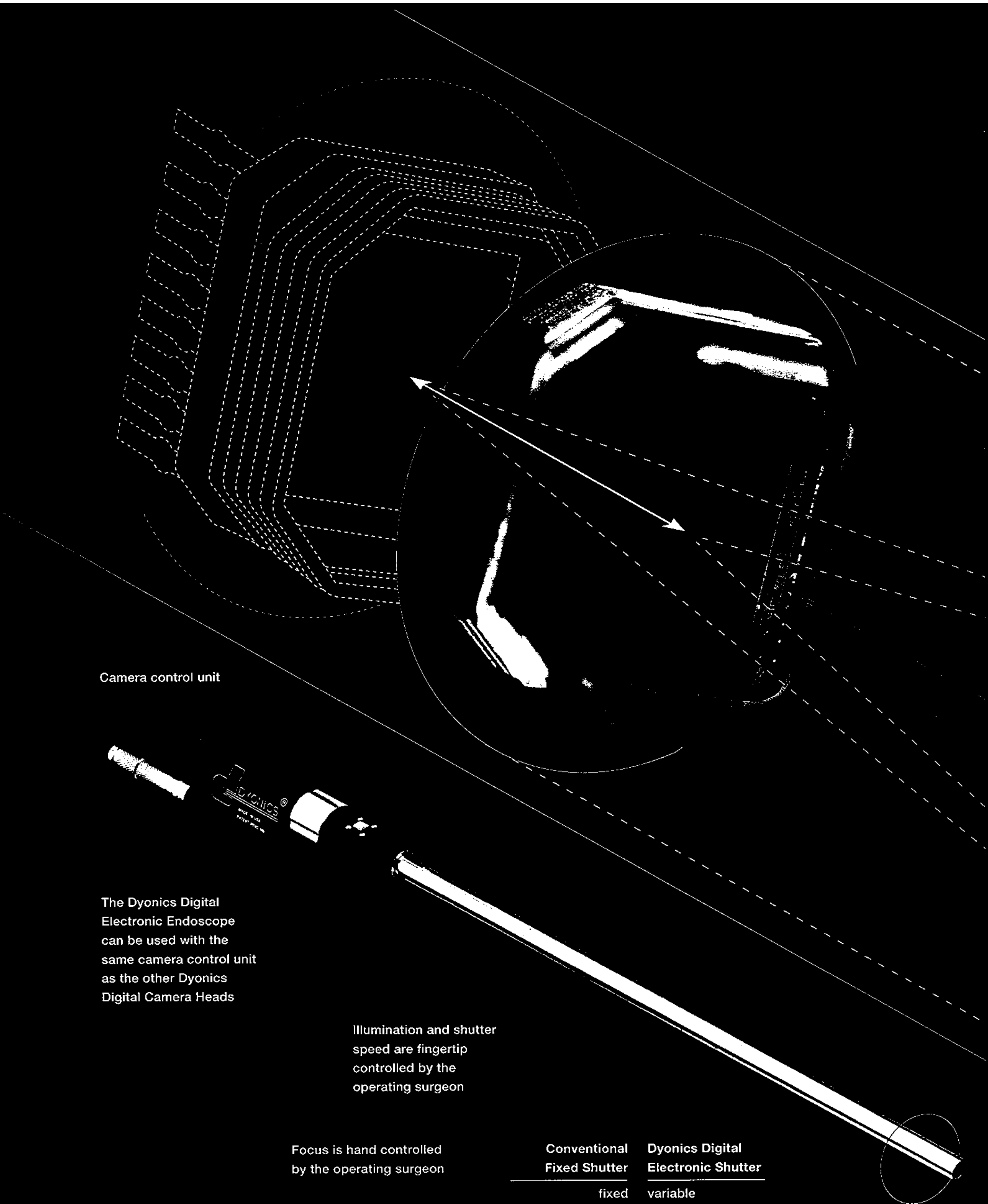


During 1994, the Group maintained its position as world leader with a sales increase of 6%, illustrating Smith & Nephew's ability to perform well in a market that has been affected by reductions in hospital expenditure, particularly in the United States. The Dyonics range was successfully launched in Japan and good growth of 39% was achieved in Europe.

The Group leads the arthroscopy instrumentation market with a 29% share, supported mainly by excellent sales of the Inteli-Jet fluid management system. Shaver and blade systems, including the new Orbit Rotatable Curved Blade, an instrument designed to reduce the number of blades needed per procedure, have also proved successful. In addition, the new Pro-Line range of manual instruments has allowed hospitals to reduce inventory and maintenance costs without sacrificing performance.

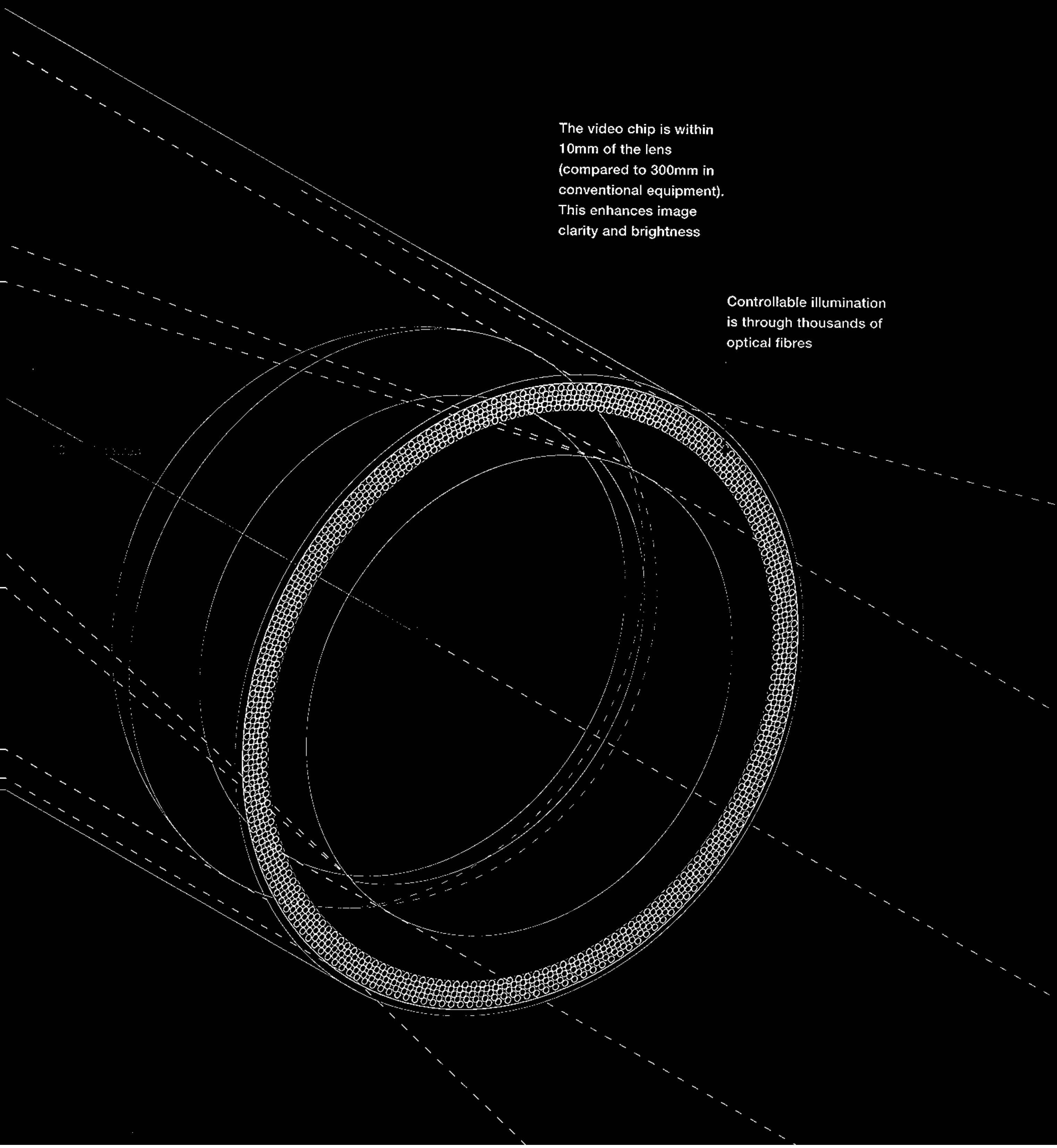
Smith & Nephew's leadership in the arthroscopy market is strengthened by its excellent range of products as well as world class service and support. Smith & Nephew's total visualisation market share has grown to 10%, and the latest product development will bring a new dimension to this marketplace. The Dyonics Digital Videocamera brings total flexibility to the operating room, as it can be used for all types of surgery and its compatibility will allow for standardisation of hospital video systems. The Dyonics camera provides high image quality and the system's modularity adds sophisticated capabilities, such as a 'picture within a picture'.

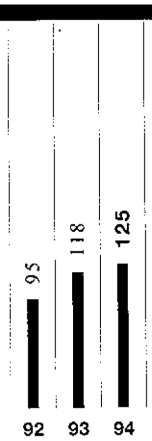
The sponsorship of a Chair in Biomedical Systems Engineering at Imperial College, London will provide access to developments in medical visualisation and medical information technology. This work allows surgeons to use computerised imaging techniques for diagnosis without surgery by investigating and photographing to aid the repair of specific medial conditions.



Conventional Fixed Shutter	Dyonics Digital Electronic Shutter
fixed	variable
1/60th second	1/60th second- 1/15,700th second 256 shutter settings (2.65 times brighter)
shutter changes at 2 x per second	shutter changes at 60 x per second

a world first





Sales
of continuing operations
£ million

Growth in this market has been boosted by another successful year of knee implant sales, one of Smith & Nephew's largest product lines

orthopaedic implants

Geographical analysis of turnover for 1994

A 21% Europe
B 65% America
C 14% Africa, Asia & Australasia

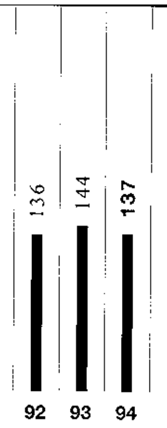
Worldwide orthopaedic implant sales for the Group increased by an underlying 7%. Progress was built on strong unit sales growth in hips, knees, bone cement and accessories.

Smith & Nephew's 1994 introduction of the Reflection Acetabular Cup, a cementless hip component, met with considerable success. Developed with the surgeon's needs and the patients quality of life in mind, Reflection is designed to reduce the debris that can lead to osteolysis (bone degeneration). This implant, either coupled with the company's newest line of hip stems, the Matrix Total Hip System or the established line of cemented stems in the Spectron Total Hip System, already has provided new business for Smith & Nephew.

A number of important line additions were made to the Matrix Total Hip System. Designed to provide technological and cost-effective solutions for total hip replacement, Matrix's comprehensive system allows surgeons to select from a variety of hip stems, all of which can be implanted with a single set of instruments. This flexible system, along with the company's new Reflection Acetabular Cup, was launched in Japan in 1994 following regulatory approval.

The Genesis Total Knee System grew solidly throughout the world at 14%, assisted by line additions which target cost-sensitive markets and instrumentation, designed to simplify and expedite the surgical procedure. As a result, Genesis has strengthened its worldwide market position.

Clinical evaluation of the Profix Total Knee System progressed well in 1994, with key surgeon involvement supporting the product launch worldwide in the first quarter of 1995. Work continues on the next generation Genesis Total Knee System and Modular Cofield Total Shoulder System, with targeted product launches in 1996.



Sales
of continuing operations
£ million

Geographical analysis of turnover for 1994

A 33% Europe
B 53% America
C 14% Africa, Asia & Australasia

other medical products

Effective product development maintains the Group in significant positions in the majority of its niche markets

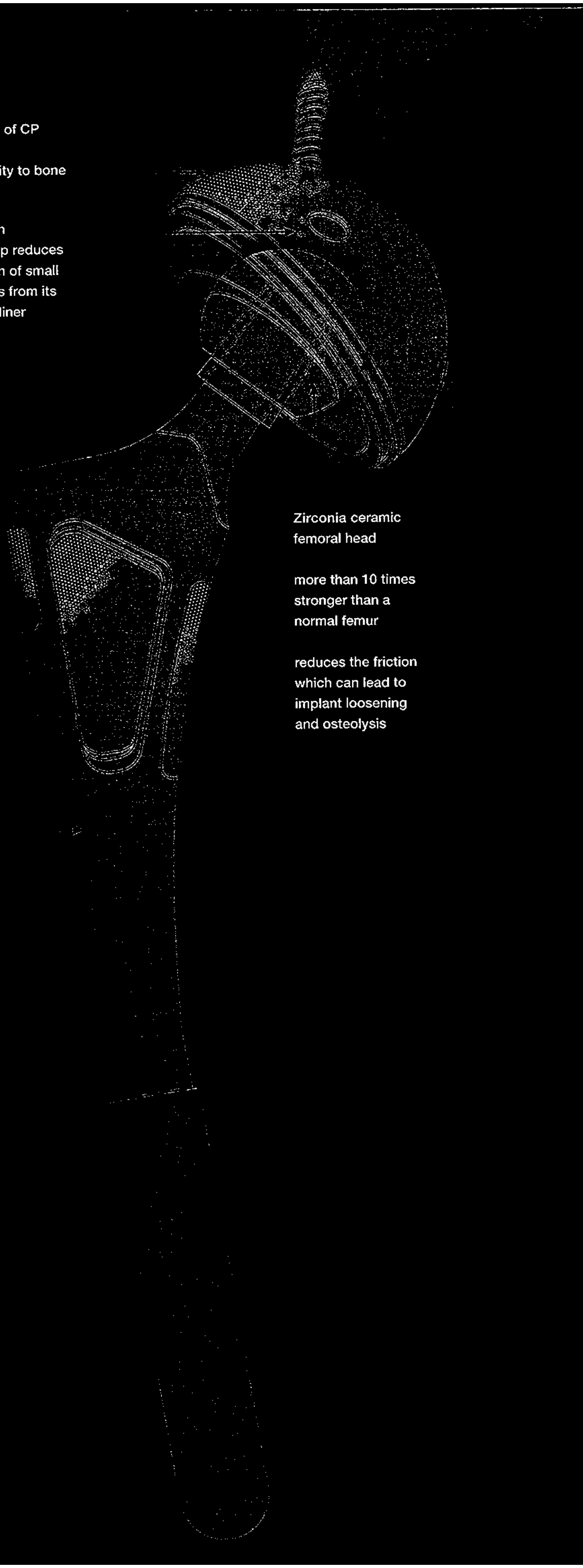
The No 3 world position in surgeons' and speciality gloves has been strengthened by the launch of four new products since 1992. Dermaguard Plus powdered and Encore powder free hypo-allergenic surgical gloves together with the DermaClean X-AM powder free hypoallergenic examination glove and Perry Clean Room range have been very successful, accounting for over 20% of total sales in 1994. Encore sales grew 68% in volume with 66% of sales outside the USA. Holland, Sweden, Spain, Australia and Canada were the top five performers. This has helped improve glove sales by 7%, an excellent achievement in this market.

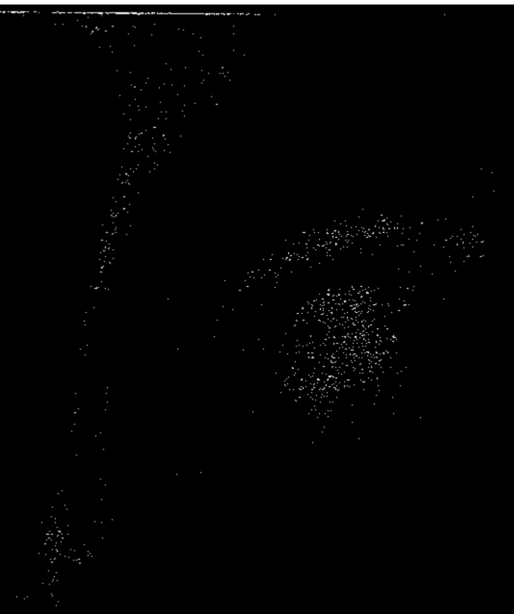
The major issue remains that of irritant and allergic reactions to gloves made from natural rubber latex. In the research area investigation is continuing into the use of enzymes and other reagents or processes, to minimise the allergenic protein content of the raw material and the search for more user friendly alternative materials such as synthetics, may provide the way for the future.

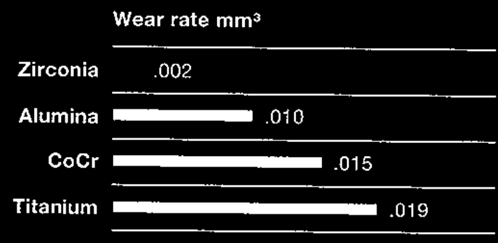
Medical specialities produced in Bartlett continue to strengthen a leadership position in otology implants. Sales of both middle ear implants, stapes and ossicular replacement prostheses increased in 1994, led by innovative products such as the Applebaum and Goldenberg implants.
The new OtoView otoscopy line was launched. The OtoView endoscopy system, used in ear surgery, offers physicians a minimally invasive technique for exploratory surgery.

The Group's medical skin care range, developed and manufactured in Florida, grew at 11%. The new line of products, targeted at the expanding nursing home population was particularly successful, and increases of 25% in Canada and 80% in Europe reflect a growing international opportunity. The strategy for this business is to continue to redevelop the range, using science and technology along with the demonstration of improved clinical outcomes, to achieve the proprietary position essential to growing our market share and developing a sustainable global position.

The sales of advanced medical dressing materials using extruded films technology showed good growth at 21%.

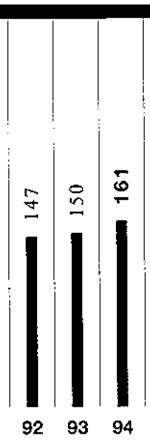

Porous beads of CP titanium for biocompatibility to bone
The Reflection acetabular cup reduces the generation of small particle debris from its polyethylene liner
Zirconia ceramic femoral head
more than 10 times stronger than a normal femur
reduces the friction which can lead to implant loosening and osteolysis
Titanium super alloy femoral stem provides high strength with flexibility for enhanced transfer of stress to surrounding bone





The Zirconia head delivers greater strength and vastly reduced wear when articulating against polyethylene

6 hip systems in 1



Sales
of continuing operations
£ million

1994 was an excellent year for Consumer Healthcare throughout the world supported by a powerful performance from Simple

consumer healthcare

Geographical analysis of turnover for 1994

A 66% Europe
B 10% America
C 24% Africa, Asia & Australasia

Worldwide sales of consumer healthcare products increased by 7%, reflecting good progress in all international markets and this business continues to be very cash generative.

The Simple toiletries range grew by 20%, with a strong contribution from the UK and an outstanding 60% growth in the Africa, Asia and Australia region.

Wrights Coal Tar Soap was acquired earlier in the year. In the UK the product complements our consumer healthcare image and will be marketed in all our consumer markets worldwide. It will be manufactured at our Corby factory and will give Smith & Nephew 7% of the UK soap market.

The Elastoplast first aid dressings range grew by 8%. Again this represents a good performance in all countries, including Australia, where Elastoplast achieved its highest ever share of 32% and in the UK we now estimate the brand holds a 50% share of the market. New international packaging has been phased in and there have been a number of line extensions, such as Elastoplast Cushioned, offering extra protection and also an innovative packaging introduction that allows consumers to apply the dressings one handed. These additions to the range, in conjunction with a good growth of our UK private label business, contributed to this performance.

The market for feminine hygiene products remains fiercely competitive. In the UK we have launched the Lil-lets Applicator Tampon with good initial results. An improved digital Lil-lets product will be launched in March 1995, an activity which will be further supported by the introduction of new packaging. In South Africa, our market leadership has been maintained.

The Smith & Nephew/ Beiersdorf arrangements on Nivea continue to develop satisfactorily and to our mutual advantage. Sales are growing strongly in all Smith & Nephew markets, with Nivea Visage in particular recording strong sales growth and increases in market share.

report of the directors

for the year ended 31 December 1994

Principal Activities The Group is a leading worldwide healthcare business whose principal activities are the manufacture and sale of medical, surgical and consumer healthcare products. Of its annual sales of £965m, 44% are in America, 38% in the UK and Continental Europe and 18% in Africa, Asia and Australasia, reflecting the geographic spread of the markets served by the Group.

The Group's customers for healthcare products are primarily hospitals many of which are organised into private or governmental buying groups. Therefore, breadth of product range is very important in Smith & Nephew's areas of operation. There is also a growing market in community care, which covers medical healthcare sales other than to hospitals. The Group through its chemist distribution channels, is well positioned to take advantage of this trend. The Group continues to improve its market shares and is world No 1 in Support Products and Arthroscopy, No 2 in Casting and Trauma Products, No 3 in Wound Management and No 5 in Implants.

Consumer healthcare products are not only an important UK business, but they also account for a significant part of the Group's business in Canada, South Africa and Australasia. Consumer healthcare products are sold primarily to retail multiple grocers and chemists.

Management and Organisation The Group operates in a variety of specialised medical and surgical product treatment areas, as well as in different country markets. In order to operate successfully in this worldwide environment, the Group has developed a cross-linked management structure involving global marketing and product development centres ('Centres of Excellence') and regional management executive committees for Europe, America, and Africa, Asia and Australasia. Each Regional Management Executive Committee is responsible for day to day operations, and in particular regional sales and marketing activities. Centres of Excellence and the Regional Management Executive Committees report through the Group Management Committee to the Chief Executive.

The Group Management Committee reviews business strategy, budgets and major investment plans, and acquisitions and disposals. Important functional areas overseen by the Committee include research and development, human resources, information management, risk management and financial and regulatory audit. An aim of the Group Management Committee is to engender an open and consultative style across the Group.

Research and Development Research and development activities of the Group are overseen by the Research Steering Group which seeks to ensure an appropriate balance between short and longer term R&D programmes. The objective is to drive real product differentiation through innovation and the continuous stimulation of Group capabilities for organic development and growth. In order to engender an independent perspective, the Scientific Advisory Panel continues to provide a regular challenge to underlying scientific and technological principles.

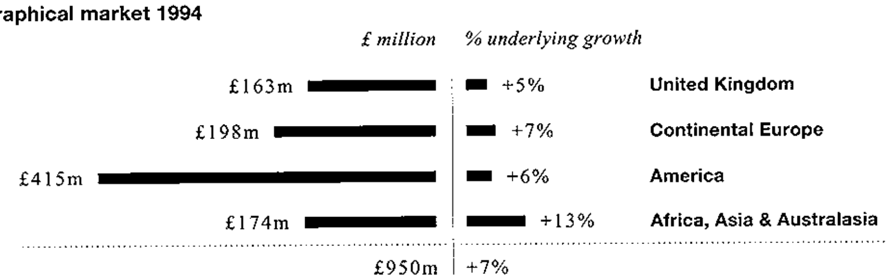
The principal locations for R&D are at the Group Research Centre in York, and the major Centres of Excellence in Memphis and Andover, in the US and Hull. The Advanced Tissue Sciences – Smith & Nephew joint venture based in La Jolla, California, began activities in the second half of 1994 to develop and market tissue-engineered cartilage replacement products.

The requirements to deliver long term data on the clinical and cost-effectiveness of products for reimbursement purposes, and the various requirements of international regulatory authorities are important concerns. The formation during 1994 of a Group Regulatory Affairs Committee is just one of the vehicles that Smith & Nephew is using to ensure that local, regional and corporate regulatory knowledge is being brought together for maximum effect.

Operating Review *Results for the year*

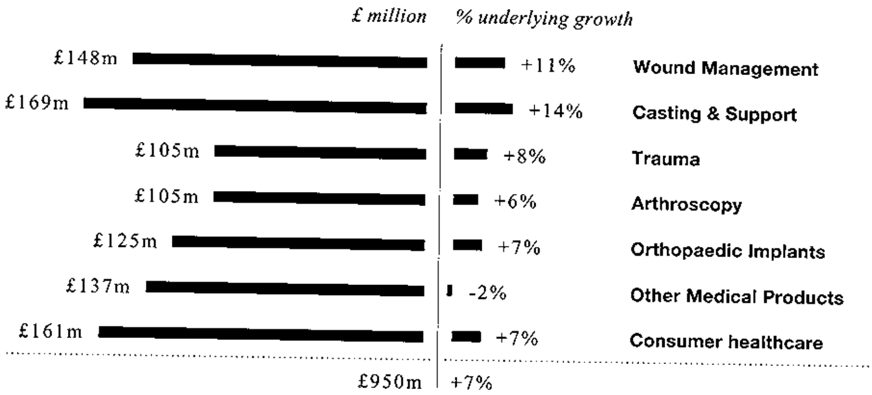
Sales increased by 2% compared with 1993, with sales of continuing operations increasing by 6% to £950m. The effect of exchange rate fluctuations on the translation of the results of international operations was unfavourable primarily due to sterling appreciating against the US, Canadian and South African currencies. Adjusting for the effect of currency translation, the underlying sales growth of continuing operations was 7%.

Sales by geographical market 1994



Healthcare sales growth improved throughout the year, particularly in Continental Europe. In the UK both Healthcare and Consumer sales grew strongly. Continental Europe had another year of consistent progress based on the strength of its Centres of Excellence products, despite difficult market conditions continuing in France. In the US the uncertainties caused by the proposed healthcare reforms eased, but the industry trend towards the consolidation of hospital and healthcare providers continues along with the increasing influence of healthcare insurance plans. These trends are placing a greater emphasis on the containment of the cost of providing healthcare, yet the Group increased sales and improved or maintained its market shares in the US. Japan, with a 33% year on year sales increase, remains a significant contributor to the progress of the region comprising Africa, Asia and Australasia. Sales growth overall accelerated to an underlying 8% in the second half of the year.

Sales by product group 1994



The five main Healthcare product groups, which now account for just over 80% of Healthcare sales, grew at 10%, demonstrating the strength of the Group's innovative products and its worldwide approach to marketing. Substantial progress was made worldwide in sales of Wound Management and Casting & Support products during the year. Trauma sales continued to grow strongly, despite a decline in spinal procedures in the US. Arthroscopy also had a very strong year outside the US, but within the US sales followed a flat market. Unit sales of implants grew strongly in the US, partly offset in value by the continued trend towards lower-priced cemented products and some slow down in the sales growth of implants in Europe.

Consumer products had an excellent year throughout the world. Sales of Simple grew strongly following its relaunch in the U K and sales of Nivea worldwide continued to benefit from the new relationship with Beiersdorf. As expected sales grew less strongly in the second half, but achieved an increase of 7% for the full year.

Operating margins for the continuing operations, before rationalisation provisions, improved from 17.9% to 18.2%, reflecting cost and efficiency savings. These more than offset pricing pressures experienced in some product markets.

Investment Capital expenditure on tangible fixed assets amounted to £60m, a similar level to that in 1993. Capital expenditure continues to represent 6% of sales. The principal project announced in 1994 was for the substantial renovation and expansion of the wound management, casting and adhesive bandaging manufacturing facility at Hull. This will involve £41m of expenditure phased over five years, £15m of which will be additional to normal levels of expenditure at Hull.

Research and development expenditure amounted to £29m, again equivalent to 3% of sales. The Group expects to continue to invest in research and development at this rate in the future. A fuller discussion on research and development is provided above. A number of intellectual property rights were acquired during the year for £5m and these have been capitalised as intangible assets.

The Group continues to invest in its selling and marketing worldwide. Start up expenditure is also being incurred in the developing markets of India and China over the next few years.

Continual cost competitiveness has to be maintained and the Group has charged £27m against profits to cover a programme of cost reduction and rationalisation of certain manufacturing facilities worldwide, along with a restructuring of distribution across Continental Europe. The cash cost of this will be £23m spread over 1995 and 1996.

Ioptex Disposal An exceptional loss of £150m was recorded on the disposal of the Ioptex intraocular lens operation. The intraocular lens market did not recover from the significant erosion in prices caused by price controls introduced by the US government in 1990 and the operation started to lose money in 1994. The majority of the exceptional loss related to goodwill which originally had been written off at the time of the acquisition. The deficit realised on net assets was £9m. Proceeds from the disposal were £11m.

Profit, Earnings per Share, Dividends and Shareholders' Funds Operating profit of the continuing operations amounted to £172.9m, before the cost of the rationalisation programme, which was a 7% increase on the previous year and in line with the increase in sales. Interest received amounted to £0.7m compared to a charge of £6.2m previously. This improvement reflects the conversion of the Convertible Preference Shares and lower average net debt in 1994. After charging the £27.4m cost of the rationalisation programme and the exceptional loss on the disposal of Ioptex of £150.3m, the result for the year became a loss of £5.5m before taxation.

Pre-tax profit before exceptional items of £172.2m represented a 9% increase on the previous year. The new Financial Reporting Standard, FRS4, has required the previous year's results to be re-stated as if the convertible preference shares then in issue were debt and the dividend thereon reclassified as interest. Adjusting for the effects of this restatement the increase in profit before exceptional items was 5%. Currency translation depressed profits by 2% such that at constant currency rates underlying profit growth was 7%. Earnings per share, before exceptional items, were 10.62 pence, an increase of 5% on the previous year.

A final dividend of 3.26 pence per ordinary share is recommended which, together with the interim dividend paid of 2.02 pence, makes a total for the year of 5.28 pence. This is an increase of 8%. Shareholders on the register at the close of business on 19 May 1995 will receive the final dividend which will be paid on 4 July 1995. It is proposed that shareholders will again be offered the opportunity to accept ordinary shares in lieu of a cash dividend. Documents will be posted to shareholders on 25 May 1995.

Taxation of £48.4m and dividends paid and proposed totalling £57.5m increase the loss before tax to a loss of £111.4m, which is taken from reserves. More than offsetting this loss is the credit that arises in reserves from re-charging the goodwill originally written off at the time of the acquisition of Ioptex to the profit and loss account on the disposal. The other major increase to shareholders' funds comprises £70m from the issue of 57,608,505 new ordinary shares issued on conversion of the preference shares, the exercise of share options and in respect of scrip dividends.

Summary of movements to shareholders' funds

	£ million
Retained Loss	(111)
Goodwill write back on the sale of Ioptex	141
Shares issued:	
Conversion of Preference Shares	64
Options and Scrip Dividends	6
Currency Translation	(2)
Increase in shareholders' funds	98

Accounts and Audit The Group's accounting policies follow generally accepted accounting principles in the United Kingdom. Apart from complying with the introduction of FRS4 there has been no material change in accounting policies during the year.

The accounts have been prepared on a going concern basis; the directors having satisfied themselves from internal forecasts and available bank facilities that the Group continues as a going concern.

The Group takes advantage of the provision of the Companies Act that enables it to publish summary financial statements in place of full annual accounts, unless shareholders request the latter. The summary financial statement version of the annual report is now received by 95% of shareholders.

The full annual accounts have been audited by Ernst & Young, Chartered Accountants, London, and received an unqualified report. Ernst & Young have expressed their willingness to continue as Auditors and a resolution proposing their re-appointment will be submitted at the Annual General Meeting.

Financial Review *Cash Flow and Facilities*

The Group converted 71% of operating profit into operating cash flow, after funding capital investments, compared with 70% last year. Operating cash flow of £122m (1993, £115m) was more than sufficient to cover interest, taxation and dividends. This, together with proceeds from disposals and share issues, enabled the Group to close the year with net cash balances of £5m.

The introduction of FRS4 has required the Group to restate the convertible preference shares in issue at the beginning of the year as if they were debt, notwithstanding the fact that they were converted into ordinary shares by March 1994. Thus opening net borrowings have increased by £65m on the published figure last year.

Net cash flow and movement in net balances during the year

	£ million
Cash in flow from operations	178
Capital investment net	(56)
Operating cash flow	122
Interest, tax and dividends	(103)
Disposals less acquisition	13
Issues of share capital	6
Net cash flow	38
Exchange adjustments	7
Conversion of preference shares	64
Opening net borrowing	(104)
Closing net cash	5

The Group has unused uncommitted bank facilities of £206m.

Capital Structure & Treasury Policy The Group protects shareholders' funds by matching, where practicable, foreign currency assets with currency liabilities. These currency liabilities take the form of either borrowings or currency swaps. At the balance sheet date the Group had borrowings of £130m, mainly in foreign currency, and cash balances of £135m, mainly in sterling. Currency swaps amounted to £224m.

Most of the borrowings are due within one year in order to take advantage of short term interest rates. Interest rate swaps are used to protect the differentials between borrowing and deposit rates as appropriate. The majority of the difference is protected through to December 1995, with some protection carrying over into 1996.

The Group trades in 92 countries and as a result manages £150m of foreign currency transactional exposure using forward foreign exchange contracts. Firm commitments are covered fully and forecasts in respect of open price lists are generally covered 50%.

Taxation The effective rate of taxation on the profits before exceptional items remains at 33%. A lower amount of tax relief is expected on the deficit realised on net assets on the Ioptex disposal and the costs of the rationalisation programme as the assets involved have lower tax values than book values.

The company is not a close company under the provisions of the Incóme and Corporation Taxes Act 1988.

Major Shareholders At the date of this report, the following interests in the ordinary share capital of the Company have been notified to the Company;
PDFM Limited and UBS International Investment London Limited 11.92%.
Sun Life Assurance Society plc 4.02%.

Corporate Governance The Board of Directors comprises five executive Directors, five non-executive Directors and with Eric Kinder as Chairman. It meets regularly during the year and has a formal schedule of matters reserved for its attention which cover key areas of the Group's business including budgets and financial statements, acquisitions and disposals, major capital expenditure, treasury matters and financial policies. Operational control is in the hands of the Chief Executive, John Robinson, assisted by the Group Management Committee. Two committees of the Board cover audit and remuneration matters.

The Audit Committee is composed of non-executive Directors, chaired by Alastair Macpherson; the Finance Director and the Internal and External Auditors attend as appropriate. It meets three times a year to review the Group's annual and interim accounts, internal financial controls and the reports of the Internal Auditor and the External Auditors.

The Remuneration Committee comprises three non-executive Directors, chaired by Sir Francis Kennedy. After taking advice, as appropriate, it approves the remuneration and other benefits, including bonus and pension arrangements, of the executive Directors and the members of the Group Management Committee. The Committee also directs the policy and operation of the share option schemes. No executive Director has a service agreement of more than one year's duration and the potential for annual bonus does not exceed 30% of salary. Non-executive Directors are appointed for terms of three years.

The Directors consider that the Company complies with the Code of Best Practice established by the Cadbury Committee, including the guideline on going concern published in 1994. The Company's Auditors, Ernst & Young, have reviewed this statement in accordance with guidance issued by the Auditing Practices Board. The Auditors have confirmed that the Directors' comments on going concern are consistent with the information they obtained during their normal audit of the accounts and have satisfied themselves that the above statement appropriately reflects the Company's compliance with the other paragraphs of the Code specified for their review.

Directors Particulars of the Directors of the Company are set out on pages 6 and 7.

Directors' emoluments for the year totalled £1,427,000 (1993 £1,395,000) of which £115,000 (1993 £255,000) were related to bonuses and £105,000 (1993 £96,000) to pension contributions. The emoluments of the Chairman, were £149,000 (1993 £127,000) and those of the Chief Executive, who is the highest paid Director who exercised his duties mainly in the United Kingdom, were £309,000 (1993 £325,000) including a bonus of £27,000 (1993 £81,000) and pension contributions of £43,000 (1993 £41,000).

In accordance with the Articles of Association, Eric Kinder, Alastair Macpherson and Christopher O'Donnell retire by rotation at the Annual General Meeting and will offer themselves for re-election.

Directors' Interests

The beneficial interests of the Directors in the ordinary shares of the Company

	31 December 1994		1 January 1994	
	Shares	Options	Shares	Options
Mr. E. Kinder	399,628	363,606	396,280	366,954
Mr. J.H. Robinson	99,990	614,888	99,990	519,888
Mr. J.R. Blair	49,548	339,216	27,838	294,216
Sir Anthony Cleaver	5,247	-	5,066	-
Mr. A.R. Fryer	78,969	364,004	76,293	324,166
Mr. P. Hooley	1,000	360,000	1,000	230,000
Sir Francis Kennedy	10,066	-	10,066	-
Dr. N.J. Lane	1,500	-	1,500	-
Mr. M.A.F. Macpherson	11,063	-	10,682	-
Mr. C.J. O'Donnell	16,286	225,000	1,033	270,000
Sir Brian Pearse	3,000	-	3,000	-

Throughout the year Eric Kinder also had a non-beneficial interest in 30,000 ordinary shares

There was no change in the interests of the Directors between 31 December 1994 and 6 March 1995. Further details of the Directors' share options are given in Note 8 to the full annual accounts.

Alastair Macpherson is a partner in Ashurst Morris Crisp, the Company's solicitors. This firm is instructed in the normal course of business and at normal business rates. Apart from this none of the Directors has a material beneficial interest in any contract to which the Company, or any of its subsidiary undertakings, was a party in 1994.

During the year the Group maintained liability insurance for its Directors and Officers.

Employees The Group operates worldwide with 12,000 employees. Employment policies are designed to provide equal opportunities for employees regardless of gender, colour, race, marital status or religion, to provide challenging careers through training and development and to provide appropriate rewards for achievement and performance. Communication is maintained with employees and where possible their views are sought on matters of common concern both through their representatives and through line managers. This is reinforced by the Group's newspaper, the Smith & Nephew Reporter and a regular Video Report.

Training and development within the Group is a priority, with the development needs of employee groups monitored. Training and development needs are met using both internal and external resources. Increasingly staff are transferred between locations both locally and between countries and continents, building their experience to the benefit of the Group and themselves. The Group encourages the employment of disabled people and particular efforts are made to retain employees who become disabled during their employment. The Group is committed to Opportunity 2000, which promotes equal opportunities for women in industry in the UK.

Environment Smith & Nephew has an established environmental policy that is integral to its business principles. The Group is committed to the protection of the environment by using renewable resources wherever possible and developing manufacturing processes and products such that any adverse effects are reduced to a practicable minimum.

More specifically it is the Group's policy:-

- to include environmental issues in all planning and decision making;
- to develop for each operation a continuous improvement programme to reduce the environmental impact of our products and services, and those of suppliers to Smith & Nephew;
- that each operating unit develops its own procedures and conducts regular audits to ensure that they are implemented;
- to pay special regard to environmental issues of the communities in which its operations are located;
- to encourage involvement in and understanding of environmental issues, particularly those related to the healthcare industry;
- to promote employee participation in voluntary environmental projects, such as recycling and waste reduction.

A Group environmental logo has been developed through a competition amongst employees throughout the world. This generated a large number of high quality entries and the winning logo is extensively used in the promotion and reporting of all matters of an environmental nature. The four leaves in the logo represent the main aspects which concern Smith & Nephew, namely energy, waste, pollution control and environmental management systems.

Smith+Nephew
Care for the Environment

Environmental achievements within the Group are recognised by an award system designed to encourage the widest possible involvement amongst employees. Measurable improvements to defined environmental standards are recognised by the award of a certificate for each of the four main aspects.

Ethical Standards Smith & Nephew employees are required to work to ethical standards which are set out in a guide for Directors and managers who in turn are responsible for ensuring that the working practices of their staff meet the required standards. This is an established policy which the Group considers fundamental to its being recognised as a responsible corporate citizen.

Charitable Contributions Group contributions to charity amounted to £1,125,000 (1993 – £1,126,000), of which £544,000 (1993 – £510,000) was in the UK. The largest single contribution of £480,000 was to the Smith & Nephew Foundation established for the funding of research, education and training in the medical and nursing professions. The Group continues to encourage sponsorship throughout the world including the Educational Trust in South Africa and is a member of Business in the Community in the UK. No political contributions were made.

By Order of the Board, 6 March 1995

M G Parsons *Secretary*

The product names referred to in this document are trademarks owned or licensed to companies within the Smith & Nephew Group.

directors' responsibilities for the accounts

The Directors are required by company law to prepare accounts for each financial year which give a true and fair view of the state of affairs of the Company and of the Group as at the end of the financial year and of the results for the year. In preparing the accounts, suitable accounting policies have been used and applied consistently, and reasonable and prudent judgements and estimates have been made. Applicable accounting standards have been followed. The Directors have satisfied themselves from internal forecasts and available Bank facilities that the Group continues as a going concern.

The Directors are also responsible for ensuring proper procedures exist for the maintenance of adequate accounting records, for safeguarding the assets of the Group and for preventing and detecting fraud and other irregularities. To this end the parent company has established financial control standards and operates an internal audit function. Annual budgets are prepared and approved by the Directors, and the Directors have reserved capital expenditure and treasury authority levels to the Board and its delegated committees. The Group operates a system of regular monthly reporting including profit and cash forecasts. The Audit Committee reviews the financial controls and reporting of the Group.

report of the auditors *to the members of Smith & Nephew plc*

We have audited the accounts on pages 34 to 56, which have been prepared under the historical cost convention and on the basis of the accounting policies set out on pages 39 and 40.

Respective responsibilities of Directors and Auditors As described above, the Company's Directors are responsible for the preparation of the accounts. It is our responsibility to form an independent opinion, based on our audit, on those accounts and to report our opinion to you.

Basis of opinion We conducted our audit in accordance with Auditing Standards issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the accounts. It also includes an assessment of the significant estimates and judgements made by the Directors in the preparation of the accounts, and of whether the accounting policies are appropriate to the Group's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the accounts are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the accounts.

Opinion In our opinion the accounts give a true and fair view of the state of affairs of the Company and of the Group at 31 December 1994 and of the loss of the Group for the year then ended and have been properly prepared in accordance with the Companies Act 1985.

Ernst & Young

Ernst & Young
Chartered Accountants,
Registered Auditor, London.

6 March 1995

group profit and loss account

for the year ended 31 December 1994	*Notes*	1994 *£ million*	1993 *£ million*
			(Restated)
Turnover	*1*		
Continuing operations		**949.9**	899.4
Discontinued operations		**14.7**	49.3
		964.6	948.7
Operating profit	*1, 2*		
Continuing operations – before exceptional items		**172.9**	161.3
– rationalisation programme	*3*	**(27.4)**	–
		145.5	161.3
Discontinued operations		**(1.4)**	2.5
		144.1	163.8
Discontinued operations – (loss)/profit on disposal	*4*	**(150.3)**	7.3
(Loss)/profit on ordinary activities before interest		**(6.2)**	171.1
Interest	*5*	**0.7**	(6.2)
(Loss)/profit on ordinary activities before taxation		**(5.5)**	164.9
Taxation	*9*	**48.4**	56.2
Attributable (loss)/profit for the year		**(53.9)**	108.7
Dividends	*10*	**57.5**	52.7
Retained (loss)/profit for the year		**(111.4)**	56.0
(Loss)/earnings per ordinary share	*12*	**(4.96)p**	10.55p

Results before exceptional items			
Profit before taxation	*11*	**172.2**	157.6
Adjusted earnings per ordinary share	*12*	**10.62p**	10.15p

A statement of the movement on reserves is set out in note 24.

group balance sheet

at 31 December 1994	*Notes*	**1994** *£ million*	1993 *£ million* *(Restated)*
Fixed assets			
Intangible assets	*13*	**8.8**	4.9
Tangible assets	*14*	**243.4**	241.7
Investments	*15*	**3.1**	5.6
		255.3	252.2
Current assets			
Stocks	*16*	**195.0**	194.5
Debtors	*17*	**260.2**	249.4
Cash and bank	*18*	**135.0**	187.4
		590.2	631.3
Creditors: amounts falling due within one year			
Convertible preference shares	*18*	**–**	65.2
Other borrowings	*18*	**112.1**	198.8
Other creditors	*19*	**222.0**	210.8
		334.1	474.8
Net current assets		**256.1**	156.5
Total assets less current liabilities		**511.4**	408.7
Creditors: amounts falling due after more than one year			
Borrowings	*18*	**17.9**	27.7
Provisions for liabilities and charges	*20*	**47.6**	33.4
		65.5	61.1
		445.9	347.6
Capital and reserves			
Called up share capital			
Equity capital	*22*	**109.1**	103.3
Non-equity capital	*22*	**0.3**	0.3
Share premium account	*24*	**93.1**	28.8
Special reserve	*24*	**–**	28.8
Other reserves	*24*	**3.2**	4.9
Profit and loss account	*24*	**240.2**	181.5
		445.9	347.6

Approved by the Board on 6 March 1995

E Kinder *Chairman* **P Hooley** *Finance Director*

E Kinder P Hooley

group cash flow

for the year ended 31 December 1994	*Notes*	**1994** **£ million**	1993 £ million (Restated)
Net cash inflow from operating activities	25	**178.1**	169.8
Returns on investments and servicing of finance			
Interest received		**11.4**	15.9
Supplementary interest paid		**–**	(30.0)
Other interest paid		**(16.4)**	(27.2)
Dividends paid		**(52.2)**	(47.2)
Net cash outflow from returns on investments and servicing of finance		**(57.2)**	(88.5)
Tax paid		**(46.0)**	(52.0)
Investing activities			
Capital investments		**(63.8)**	(66.1)
Disposal of fixed assets		**8.0**	11.4
Acquisitions		**(3.0)**	–
Disposals		**15.8**	34.1
Net cash outflow from investing activities		**(43.0)**	(20.6)
Net cash inflow before financing		**31.9**	8.7
Financing	25		
Issue of ordinary share capital		**70.1**	18.7
New short term loans		**47.0**	17.0
Repayment of amounts borrowed		**(86.1)**	(117.1)
Net cash inflow/(outflow) from financing		**31.0**	(81.4)
Increase/(decrease) in cash and cash equivalents	25	**62.9**	(72.7)

group statement of total recognised gains and losses

for the year ended 31 December 1994	**1994** ***£ million***	1993 *£ million*
(Loss)/profit for the financial year	**(53.9)**	108.7
Currency translation differences on foreign currency net investments	**(2.3)**	(13.1)
Total losses and gains related to the year	**(56.2)**	95.6

group reconciliation of movements in shareholders' funds

for the year ended 31 December 1994	**1994** ***£ million***	1993 *£ million*
(Loss)/profit for the financial year	**(53.9)**	108.7
Dividends	**57.5**	52.7
Retained (loss)/profit for the year	**(111.4)**	56.0
Currency translation	**(2.3)**	(13.1)
Issue of shares	**70.1**	18.7
Scrip dividend	**2.6**	1.2
Goodwill on acquisitions	**(1.7)**	–
Goodwill on disposals	**141.0**	2.6
Net addition to shareholders' funds	**98.3**	65.4
Opening shareholders' funds	**347.6**	282.2
Closing shareholders' funds	**445.9**	347.6

parent company balance sheet

at 31 December 1994	Notes	1994 £ million	1993 £ million
Fixed assets			
Tangible assets	*14*	**3.1**	2.7
Investments	*15*	**420.1**	417.7
		423.2	420.4
Current assets			
Debtors	*17*	**473.8**	274.9
Cash and bank	*18*	**76.3**	116.7
		550.1	391.6
Creditors: amounts falling due within one year			
Borrowings	*18*	**89.5**	149.2
Other creditors	*19*	**345.4**	265.8
		434.9	415.0
Net current assets/(liabilities)		**115.2**	(23.4)
Total assets less current liabilities		**538.4**	397.0
Creditors: amounts falling due after more than one year			
Borrowings	*18*	**2.4**	2.5
Provisions for liabilities and charges	*20*	**1.5**	2.8
		3.9	5.3
		534.5	391.7
Capital and reserves			
Called up share capital			
Equity share capital	*22*	**109.1**	103.3
Non-equity share capital	*22*	**0.3**	0.3
Share premium account	*24*	**93.1**	28.8
Special reserve	*24*	**–**	28.8
Other reserves	*24*	**2.6**	2.6
Profit and loss account	*24*	**329.4**	227.9
		534.5	391.7

Approved by the Board on 6 March 1995

E Kinder *Chairman* **P Hooley** *Finance Director*

accounting policies

The accounts have been prepared under the historical cost convention and in accordance with applicable accounting standards.

Consolidation The consolidated accounts include the accounts of the Company and the accounts of all the subsidiary and associated undertakings during the year ended 31 December 1994 for the periods during which they were members of the Group.

Goodwill, representing the excess of purchase consideration over fair value of net tangible assets acquired, is written off direct to reserves in the year of acquisition. Goodwill previously written off to reserves is included in the calculation of profits and losses on disposals.

Intangible fixed assets Purchased patents, licences and distribution rights are capitalised and amortised over the economic life of the right concerned. Purchased trademarks are capitalised but are not amortised while their value is maintained by investments in advertising and marketing.

Associated undertakings Associated undertakings are those companies in which the Group has a beneficial interest of between 20% and 50% in the equity capital and where the Group exercises significant influence over commercial and financial policy decisions. The consolidated balance sheet includes the Group's share of the underlying net assets of associated undertakings.

Foreign currencies Balance sheet items of overseas companies and foreign currency borrowings are translated into sterling at the year end rates of exchange. Profit and loss items and the cash flows of overseas subsidiary and associated undertakings are translated at the average rates for the year.

Exchange differences on the translation at closing rates of exchange of the opening net assets of overseas subsidiary and associated undertakings are recorded as adjustments to reserves. Where foreign currency borrowings or swaps are used to finance or hedge Group equity investments, the difference on translation of these borrowings or swaps is offset as an adjustment to reserves. The differences arising between the translation of profits at average and closing rates of exchange are also recorded as adjustments to reserves. All other exchange differences are dealt with in arriving at profit before taxation.

Depreciation Depreciation is charged on the following bases:
Freehold and long leasehold land (leases 50 years or over) is not depreciated.
Freehold and long leasehold buildings are depreciated on a straight-line basis at between 1% and 5% per annum.
Short leasehold land and buildings (leases of under 50 years) are depreciated by equal annual instalments over the term of the lease.
Plant and equipment are depreciated over lives ranging between 3 and 20 years by equal annual instalments to write down the assets to their estimated disposal value at the end of their working lives.

Leases Assets held under finance leases are capitalised as tangible fixed assets and depreciated accordingly. The capital element of future lease payments is included in borrowings and interest is charged to profit before taxation on a reducing balance basis over the term of the lease. Rentals under operating leases are charged to operating profit as incurred.

Stocks Finished goods and work-in-progress are valued at factory cost, including appropriate overheads on a first in first out basis. Raw materials are valued at purchase price and all stocks are reduced to net realisable value where lower.

Deferred taxation Deferred taxation is provided under the liability method on timing differences between tax and accounting treatments where these are likely to crystallise in the foreseeable future. Deferred taxation is not provided on undistributed profits retained overseas.

Research and development Revenue expenditure on research and development and on patents and trademarks is written off as incurred.

Post-retirement benefits The Group's major pension plans are of the defined benefit type. For these plans, costs are charged to operating profit so as to spread the expense of providing future pensions to employees over their working lives with the Group. Where defined contribution plans operate the contributions to these plans are charged to operating profit as they become payable.

Where the Group provides healthcare benefits after retirement the expected cost of these is charged to operating profit over the employees' working lives with the Group.

Restatement of comparatives Comparative figures have been restated in accordance with Financial Reporting Standard No. 4 ("Capital Instruments") so as to reclassify the convertible preference shares issued by Smith & Nephew Finance NV from minority interests to net borrowings. Dividends payable on these preference shares have been reclassified from minority interests to interest payable. All the preference shares were converted or redeemed in full by 31 December 1994.

notes to the accounts

1 Segmental analysis

Analysis by activity	Turnover 1994 £ million	Operating profit 1994 £ million	Operating assets 1994 £ million	Turnover 1993 £ million	Operating profit 1993 £ million	Operating assets 1993 £ million
Healthcare	**788.9**	**124.5**	**431.5**	749.8	143.0	423.4
Consumer	**161.0**	**21.0**	**67.8**	149.6	18.3	70.5
	949.9	**145.5**	**499.3**	899.4	161.3	493.9
Discontinued operations	**14.7**	**(1.4)**	**1.9**	49.3	2.5	19.2
	964.6	**144.1**	**501.2**	948.7	163.8	513.1

Exceptional rationalisation programme costs of £27.4m have been charged to Healthcare. The 1993 analysis of operating profit has been restated following a refinement in the basis of allocation of expenses. Healthcare profits increased and Consumer profits declined by £1.6m.

Analysis by geographic origin	Turnover 1994 £ million	Operating profit 1994 £ million	Operating assets 1994 £ million	Turnover 1993 £ million	Operating profit 1993 £ million	Operating assets 1993 £ million
United Kingdom	**238.6**	**40.5**	**145.4**	219.7	36.1	125.2
Continental Europe	**205.5**	**17.0**	**88.2**	190.1	25.4	83.8
America	**469.9**	**71.5**	**198.3**	457.7	81.5	213.7
Africa, Asia & Australasia	**151.4**	**16.5**	**67.4**	135.9	18.3	71.2
	1,065.4	**145.5**	**499.3**	1,003.4	161.3	493.9
Discontinued operations	**17.1**	**(1.4)**	**1.9**	52.1	2.5	19.2
	1,082.5	**144.1**	**501.2**	1,055.5	163.8	513.1
Less intergroup sales	**(117.9)**			(106.8)		
	964.6	**144.1**	**501.2**	948.7	163.8	513.1

Exceptional rationalisation programme costs of £27.4m have been charged as follows: UK £2.2m, Continental Europe £7.2m, America £14.1m and Africa, Asia & Australasia £3.9m.

Operating assets comprise fixed assets, stocks and debtors less creditors and provisions (other than net borrowings, taxation and dividends).

Analysis of turnover by geographic market	1994 £ million	1993 £ million
United Kingdom	**162.7**	154.4
Continental Europe	**197.7**	186.5
America	**415.2**	405.4
Africa, Asia & Australasia	**174.3**	153.1
	949.9	899.4
Discontinued operations	**14.7**	49.3
	964.6	948.7

1 Segmental analysis continued

Analysis of turnover by product	1994 £ million	1993 £ million
Wound management	**147.5**	136.4
Casting and support	**169.5**	152.4
Trauma	**104.7**	98.4
Arthroscopy	**105.2**	100.9
Orthopaedic implants	**124.7**	117.8
Other medical products	**137.3**	143.9
Healthcare	**788.9**	749.8
Consumer	**161.0**	149.6
	949.9	899.4
Discontinued operations	**14.7**	49.3
	964.6	948.7

2 Operating profit

	Continuing operations 1994 £ million	Discontinued operations 1994 £ million	Total 1994 £ million	Continuing operations 1993 £ million	Discontinued operations 1993 £ million	Total 1993 £ million
Turnover	**949.9**	**14.7**	**964.6**	899.4	49.3	948.7
Cost of sales	**(435.9)**	**(6.2)**	**(442.1)**	(400.4)	(25.6)	(426.0)
Gross profit	**514.0**	**8.5**	**522.5**	499.0	23.7	522.7
Selling and distribution costs	**(266.9)**	**(6.5)**	**(273.4)**	(242.9)	(13.4)	(256.3)
Administrative expenses	**(78.0)**	**(2.8)**	**(80.8)**	(71.3)	(6.2)	(77.5)
Research & development costs	**(28.4)**	**(0.6)**	**(29.0)**	(27.5)	(1.6)	(29.1)
Associated undertakings	–	–	–	1.2	–	1.2
Other income net of expenses	**4.8**	–	**4.8**	2.8	–	2.8
Operating profit	**145.5**	**(1.4)**	**144.1**	161.3	2.5	163.8

Exceptional rationalisation programme costs of £27.4m have been allocated as follows: cost of sales £13.9m, selling and distribution £7.4m, administration £6.1m.

Operating profit is stated after charging/(crediting):	1994 £ million	1993 £ million
Amortisation of intangibles	**0.5**	0.5
Depreciation	**36.1**	35.5
Loss/(profit) on disposal of fixed assets	**0.3**	(3.2)
Operating lease rentals: land and buildings	**6.8**	6.6
plant and equipment	**4.2**	4.2
Auditors' remuneration	**1.3**	1.3

Payments made to Group Auditors in the UK for non-audit services amounted to £0.4m (1993 £0.4m); outside the UK £0.6m (1993 £0.8m). These fees relate to tax and other advisory services.

3 Rationalisation programme

Represents provisions to cover the costs of a programme of cost reduction and rationalisation of certain manufacturing facilities worldwide, along with the restructuring of distribution in Continental Europe.

4 (Loss)/profit on disposal

The loss on disposal of discontinued operations relates to the sale of the Ioptex intraocular lens operation and includes goodwill previously written off to reserves of £141.0m. The profit on disposal of discontinued operations in 1993 consists of profits on the sale of the UK ophthalmic solutions and Australian plastics businesses less the loss on the US dental needles business; it includes goodwill previously written off to reserves of £2.6m.

5 Interest

	1994 *£ million*	1993 *£ million*
Interest receivable	**11.5**	17.8
Interest payable:		
On bank borrowings	**9.1**	12.1
On convertible preference shares	**0.1**	5.7
On other borrowings wholly repayable within five years	**1.3**	5.4
On other borrowings wholly or partly repayable after five years	**0.3**	0.8
	10.8	24.0
	0.7	(6.2)

6 Employees

The average number of employees during the year was:	1994	1993
United Kingdom	**3,904**	4,179
Continental Europe	**1,528**	1,539
America	**4,288**	4,646
Africa, Asia & Australasia	**2,503**	2,735
	12,223	13,099

Staff costs during the year amounted to:	*£ million*	*£ million*
Wages and salaries	**205.0**	218.8
Social security costs	**23.5**	24.7
Other pension costs (note 28)	**5.8**	6.2
	234.3	249.7

7 Directors' emoluments

	1994 £000	1993 £000
Fees	**120**	115
Salaries and benefits	**1,087**	929
Pension contributions	**105**	96
Bonuses	**115**	255
	1,427	1,395
Pension paid to former Director	**34**	35

The bonuses of executive Directors are related to three criteria; real year on year growth in adjusted earnings per share, achievement of profit budget, and year on year growth in profit. In the case of executive Directors with divisional responsibilities the profit measure is the operating profit of their divisions adjusted for usage of capital employed. For the Chief Executive and the Finance Director the profit measure is Group profit before exceptional items and currency translation. executive Directors are also granted options under the Executive and Employee Share Option Schemes. Details of options held by executive Directors and those granted and exercised in 1994 are set out in note 8. The executive Directors are members of pension plans which in the UK broadly accrue two thirds of the average of their final two years' salary as a pension after thirty years' service. In addition, unfunded provision has been made for certain Directors' pension benefits, the cost of which was £84,000 (1993 – £64,000).

The emoluments of the Chairman and the highest paid Director who exercised his duties mainly in the UK, are:

	1994 £000	1993 £000
The Chairman	**149**	127
The Chief Executive, who is the highest paid UK Director:		
Salary and benefits	**239**	203
Pension contribution	**43**	41
Bonus	**27**	81
Total emoluments of the Chief Executive	**309**	325

The following table shows the number of Directors who exercised their duties mainly in the UK, including those above, and whose emoluments (excluding pension contributions) fall within the ranges below:

	Number within the range 1994	1993		Number within the range 1994	1993
£10,001 - £15,000	**–**	2	£155,001 - £160,000	**–**	1
£15,001 - £20,000	**5**	3	£165,001 - £170,000	**1**	–
£125,001 - £130,000	**1**	1	£170,001 - £175,000	**1**	1
£140,001 - £145,000	**–**	1	£265,001 - £270,000	**1**	–
£145,001 - £150,000	**1**	–	£280,001 - £285,000	**–**	1

8 Directors' share options

Options: exercise prices below market price	Number of shares under option: 1 January 1994	Granted	Exercised	31 December 1994	Weighted average exercise price pence
Mr E Kinder	366,954			366,954	134.24
7 September 1994 at 154p			(3,348)	(3,348)	131.40
	366,954	–	(3,348)	363,606	134.27
Mr J H Robinson	439,888	–	–	439,888	118.22
Mr J R Blair	279,216	–	–	279,216	135.05
Mr A R Fryer	294,166			294,166	118.90
12 September 1994 at 148p			(2,962)	(2,962)	121.50
14 September 1994		2,800		2,800	123.20
	294,166	2,800	(2,962)	294,004	118.91
Mr P Hooley	140,000	–	–	140,000	138.14
Mr C J O'Donnell	180,000			180,000	124.94
9 September 1994 at 152p			(30,000)	(30,000)	137.00
9 September 1994 at 152p			(50,000)	(50,000)	93.50
	180,000	–	(80,000)	100,000	137.05

Options: exercise prices above market price	1 January 1994	Granted	Exercised	31 December 1994	Weighted average exercise price pence
Mr J H Robinson	80,000			80,000	168.00
15 August 1994		95,000		95,000	154.00
	80,000	95,000	–	175,000	160.40
Mr J R Blair	15,000			15,000	168.00
15 August 1994		45,000		45,000	154.00
	15,000	45,000	–	60,000	157.50
Mr A R Fryer	30,000			30,000	168.00
15 August 1994		40,000		40,000	154.00
	30,000	40,000	–	70,000	160.00
Mr P Hooley	90,000			90,000	168.00
15 August 1994		130,000		130,000	154.00
	90,000	130,000	–	220,000	159.73
Mr C J O'Donnell	90,000			90,000	168.00
15 August 1994		35,000		35,000	154.00
	90,000	35,000	–	125,000	164.08

The market price of the shares at 31 December 1994 was 153p, and this price has been used for determining whether exercise prices were below or above market. The range in the market price of the Company's shares during the year was 137p to 159p.

Under the Executive Share Option Scheme, Directors may in any ten year period, be granted over a four year period, options over shares in the Company of value up to four times their basic salary. The share options are exercisable any time between the third and tenth anniversary of the date of the grant of particular options.

9 Taxation

	1994 £ million	1993 £ million
United Kingdom taxation		
Corporation tax at 33% (1993 – 33%)	**45.1**	32.8
Double taxation relief	**(26.3)**	(19.6)
Deferred taxation	**0.1**	4.2
Advance corporation tax	**0.7**	1.8
Adjustments in respect of prior years	**–**	(1.8)
	19.6	17.4
Overseas taxation		
Current taxation	**36.4**	34.8
Deferred taxation	**(4.7)**	5.3
Adjustments in respect of prior years	**(2.9)**	(1.3)
	28.8	38.8
Taxation charged	**48.4**	56.2

If full provision had been made for deferred tax, the tax charge would have decreased by £3.5m (1993 – £0.6m) as follows:

	1994 £ million	1993 £ million
Fixed asset timing differences	**(0.3)**	(1.3)
Other timing differences	**3.1**	0.1
Advance corporation tax	**0.7**	1.8
	3.5	0.6

The tax charge is reduced by £6.8m as a consequence of the rationalisation programme and by £1.6m (1993 – increased by £3.2m) as a consequence of the exceptional loss/profit on disposal.

10 Dividends

	1994 £ million	1993 £ million
Ordinary interim of 2.02p paid 12 December 1994 (1993 – 1.89p)	**22.0**	19.9
Proposed ordinary final of 3.26p payable 4 July 1995 (1993 – 3.02p)	**35.5**	32.8
	57.5	52.7

Non-equity preference dividends amounting to £10,000 were paid in both 1994 and 1993.

11 Results before exceptional items

In order to provide a trend measure of performance, profit before tax is adjusted below to exclude exceptional items and earnings per share has been recalculated as set out in note 12.

	1994 £ million	1993 £ million
(Loss)/profit on ordinary activities before tax	**(5.5)**	164.9
Adjustments		
Rationalisation programme	**27.4**	–
Discontinued operations: loss/(profit) on disposal	**150.3**	(7.3)
Total adjustments	**177.7**	(7.3)
Profit before tax and exceptional items	**172.2**	157.6
Tax on profit before exceptional items	**56.8**	53.0

12 Earnings per ordinary share

The calculation of (loss)/earnings per ordinary share is based on the loss, after deducting preference dividends, of £53.9m (1993 – earnings of £108.7m) and on 1,087m ordinary shares being the weighted average number of shares in issue during the year (1993 – 1,030m).

Adjusted earnings per share is calculated as follows:	1994 Pence per share	1993 Pence per share
(Loss)/earnings per ordinary share	**(4.96)**	10.55
Effect of profit adjustments (note 11)	**16.35**	(0.71)
Taxation effect of profit adjustments (note 9)	**(0.77)**	0.31
Adjusted earnings per ordinary share	**10.62**	10.15

13 Intangible fixed assets

Group	£ million
Cost	
At 1 January 1994	5.4
Exchange adjustment	(0.3)
Additions	4.7
At 31 December 1994	**9.8**
Depreciation	
At 1 January 1994	0.5
Exchange adjustment	–
Charge for the year	0.5
At 31 December 1994	**1.0**
Net book amounts	
At 31 December 1994	**8.8**
At 31 December 1993	4.9

14 Tangible fixed assets

Group	Land and buildings Freehold £ million	Land and buildings Leasehold £ million	Plant and equipment £ million	In course of construction £ million	Total £ million
Cost					
At 1 January 1994	86.4	6.0	296.7	25.8	414.9
Exchange adjustment	(2.4)	–	(4.1)	(0.7)	(7.2)
Additions	4.4	4.2	26.2	25.3	60.1
Disposals	(3.7)	(1.8)	(17.4)	–	(22.9)
Disposal of operations	(2.5)	–	(6.2)	(0.3)	(9.0)
Transfers	6.2	3.3	21.3	(30.8)	–
At 31 December 1994	**88.4**	**11.7**	**316.5**	**19.3**	**435.9**
Depreciation					
At 1 January 1994	12.4	1.3	159.5	–	173.2
Exchange adjustment	(0.3)	–	(2.1)	–	(2.4)
Charge for the year	1.8	0.3	34.0	–	36.1
Disposals	(0.7)	(0.6)	(13.6)	–	(14.9)
Disposal of operations	–	–	(3.0)	–	(3.0)
Provision for rationalisation	–	–	3.5	–	3.5
Transfers	0.4	–	(0.4)	–	–
At 31 December 1994	**13.6**	**1.0**	**177.9**	–	**192.5**
Net book amounts					
At 31 December 1994	**74.8**	**10.7**	**138.6**	**19.3**	**243.4**
At 31 December 1993	74.0	4.7	137.2	25.8	241.7

Leases with less than 50 years to run amounted to £6.8m (1993 – £4.4m). Included in the amounts above are assets held under finance leases with a net book amount of £3.9m (1993 – £0.5m).

Parent company

Included above are tangible fixed assets of the parent company having a cost of £4.4m (1993 – £3.8m) and net book amount of £3.1m (1993 – £2.7m).

15 Fixed assets – investments

	Group associated undertakings £ million	Group trade investments £ million	Group Total £ million	Parent subsidiary undertakings £ million
At 1 January 1994	3.6	2.0	5.6	417.7
Exchange adjustment	(0.2)	(0.1)	(0.3)	–
Additions	–	–	–	3.7
Disposals and transfers	(2.2)	–	(2.2)	(1.3)
Retained profit	–	–	–	–
At 31 December 1994	**1.2**	**1.9**	**3.1**	**420.1**

Principal subsidiary undertakings and principal associated undertakings are listed on page 56. The trade investment comprises a 16% interest in SpineTech Inc. incorporated in the USA.

16 Stocks

	Group 1994 £ million	Group 1993 £ million
Raw materials and consumables	**47.9**	46.8
Work-in-progress	**20.0**	19.2
Finished goods and goods for resale	**127.1**	128.5
	195.0	194.5

17 Debtors

	Group 1994 £ million	Group 1993 £ million	Parent 1994 £ million	Parent 1993 £ million
Amounts falling due within one year:				
Trade and other debtors	**223.3**	216.3	**5.0**	7.2
Amounts owed by subsidiary undertakings	–	–	**454.5**	254.6
Amounts owed by associated undertakings	**0.7**	1.7	–	–
Prepayments and accrued income	**13.3**	14.9	**1.3**	2.4
	237.3	232.9	**460.8**	264.2
Amounts falling due after more than one year:				
Pension prepayments	**6.2**	5.8	–	–
Deferred tax (note 21)	**3.7**	–	–	–
Advance corporation tax	**13.0**	10.7	**13.0**	10.7
	260.2	249.4	**473.8**	274.9

18 Borrowings

Net Borrowings

	Group 1994 £ million	Group 1993 £ million	Parent 1994 £ million	Parent 1993 £ million
Gross borrowings:				
Convertible preference shares	–	65.2	–	–
Other due within one year	**112.1**	198.8	**89.5**	149.2
Due after one year	**17.9**	27.7	**2.4**	2.5
	130.0	291.7	**91.9**	151.7
Cash and bank	**(135.0)**	(187.4)	**(76.3)**	(116.7)
Net (cash)/borrowings	**(5.0)**	104.3	**15.6**	35.0
Of which secured borrowings:				
On cash	**5.5**	11.5	–	–
On fixed and current assets	**4.2**	1.9	–	–
	9.7	13.4	–	–

At the year end, cash of £7.0m (1993 – £14.5m) was pledged as security on borrowings of £5.5m (1993 – £11.5m).

18 Borrowings continued

Gross borrowings	Group 1994 £ million	Group 1993 £ million	Parent 1994 £ million	Parent 1993 £ million
Bank loans and overdrafts	**117.1**	210.0	**89.5**	149.2
Other loans:				
Wholly repayable within five years				
Convertible preference shares	**–**	65.2	**–**	–
14% US $ Promissory Note 1991/95	**5.4**	11.5	**–**	–
Other	**2.9**	2.5	**–**	–
	8.3	79.2	**–**	–
Wholly repayable after five years				
5½% US $ Convertible Bonds 2000	**2.0**	2.0	**2.0**	2.0
Other	**2.6**	0.5	**0.4**	0.5
	4.6	2.5	**2.4**	2.5
	130.0	291.7	**91.9**	151.7

Bank loans and overdrafts represent drawings under committed and uncommitted facilities of £37m and £300m respectively. Interest rates on these drawings ranged from 2.25% to 17.5% and reflect market rates of the currencies and terms concerned.

The Group has currency swaps which are revalued at year end exchange rates. The gross sterling equivalents of £226m (1993 – £144m) receivable and £223.5m (1993 – £148.3m) payable have been netted. The balance of £2.5m is included in cash (1993 – £4.3m in borrowings).

The 5½% US $ Convertible Bonds are convertible into ordinary shares at 109 pence per share at a fixed exchange rate of US $1.4202 to £1. If not converted, the bonds are repayable in the year 2000 at the latest.

Gross borrowings are repayable as follows:	Group 1994 £ million	Group 1993 £ million	Parent 1994 £ million	Parent 1993 £ million
Within one year:				
Bank loans and overdrafts	**105.4**	192.6	**89.5**	149.2
Other loans	**6.7**	71.4	**–**	–
Total within one year	**112.1**	264.0	**89.5**	149.2
Bank loans and overdrafts:				
after one year and within two years	**6.5**	0.5	**–**	–
after two years and within five years	**4.6**	15.5	**–**	–
after five years	**0.6**	1.4	**–**	–
	11.7	17.4	**–**	–
Other loans:				
after one year and within two years	**0.4**	6.9	**–**	–
after two years and within five years	**1.2**	0.8	**–**	–
after five years	**4.6**	2.6	**2.4**	2.5
	6.2	10.3	**2.4**	2.5
Total after one year	**17.9**	27.7	**2.4**	2.5
	130.0	291.7	**91.9**	151.7

19 Creditors: amounts falling due within one year

Other creditors	Group 1994 £ million	Group 1993 £ million	Parent 1994 £ million	Parent 1993 £ million
Trade creditors	**93.6**	94.9	**1.0**	0.8
Amounts owed to subsidiary undertakings	–	–	**275.2**	201.8
Amounts owed to associated undertakings	–	0.1	–	–
Social security costs and other taxes	**12.3**	11.7	–	0.1
Accruals and deferred income	**39.1**	33.5	**2.5**	3.0
Current taxation	**41.5**	32.1	**31.2**	27.3
Ordinary share dividend	**35.5**	32.8	**35.5**	32.8
Convertible preference dividend	–	5.7	–	–
	222.0	210.8	**345.4**	265.8

20 Provisions for liabilities and charges

Group	Deferred taxation £ million	Post retirement healthcare £ million	Other £ million	Total £ million
At 1 January 1994	1.3	7.5	24.6	33.4
Exchange adjustment	0.2	(0.2)	(0.2)	(0.2)
Acquisitions	–	–	0.3	0.3
Profit and loss account	(5.5)	0.5	26.7	21.7
Utilisation	0.3	(0.2)	(10.2)	(10.1)
Transfer to debtors	3.7	–	(1.2)	2.5
At 31 December 1994	**–**	**7.6**	**40.0**	**47.6**
Parent company				
At 1 January 1994	1.7	–	1.1	2.8
Profit and loss account	(0.9)	–	(0.4)	(1.3)
At 31 December 1994	**0.8**	**–**	**0.7**	**1.5**

Other provisions include £31.0m (1993 – £11.4m) relating to the rationalisation and restructuring.

21 Deferred taxation

Deferred tax (asset)/liability is analysed as follows:

Group	Amount provided 1994 £ million	Amount provided 1993 £ million	Full potential liability 1994 £ million	Full potential liability 1993 £ million
Fixed asset timing differences	**3.0**	2.4	**27.3**	26.4
Other timing differences	**(6.7)**	(1.1)	**(16.0)**	(7.3)
Advance corporation tax	–	–	**(3.5)**	(2.8)
	(3.7)	1.3	**7.8**	16.3

Parent company				
Fixed asset timing differences	–	–	**0.1**	0.1
Other timing differences	**0.8**	1.7	**0.8**	1.6
Advance corporation tax	–	–	**(0.5)**	(1.0)
	0.8	1.7	**0.4**	0.7

22 Called up share capital

Authorised	1994 Shares '000	1994 £ million	1993 Shares '000	1993 £ million
Ordinary shares 10p	**1,495,500**	**149.5**	1,495,500	149.5
3.85% Cumulative Preference Shares £1	**450**	**0.5**	450	0.5
		150.0		150.0

Allotted, issued and fully paid

Equity capital

Ordinary shares 10p	Shares '000	£ million
At 1 January 1994	1,033,083	103.3
Conversion of preference shares	50,629	5.1
Scrip dividends	1,862	0.2
Share options and long service awards	5,117	0.5
At 31 December 1994	**1,090,691**	**109.1**
Non-equity capital		
3.85% Cumulative Preference Shares £1		
At 31 December 1994 and 1 January 1994	**269**	**0.3**
Total called up share capital at 31 December 1994		**109.4**

The 3.85% Cumulative Preference Shares are non-voting and carry preferential rights to dividends and distribution on winding up.

Shares issued during the year include 50.6 million resulting from the conversion of the 8¾% Guaranteed Redeemable Preference Shares 2004 issued by Smith & Nephew Finance NV.

23 Share option schemes

At 31 December 1994 30,015,000 (1993 – 35,492,000) of the authorised but unissued ordinary shares of 10p were reserved in respect of the following options:

	Exercisable in stages between	Exercise prices per share range between	Thousands of shares the subject of options
Employee Share Option Schemes	1995 - 2000	94.4p and 164p	16,054
Executive Share Option Schemes	1995 - 2004	93.5p and 168p	13,961
			30,015

24 Reserves

Group	Share premium £ million	Special reserve £ million	Other reserves £ million	Profit and loss account £ million
At 1 January 1994	28.8	28.8	4.9	181.5
Currency translation	–	–	(0.1)	(2.2)
Goodwill on acquisitions	–	–	–	(1.7)
Goodwill on disposals	–	–	–	141.0
Retained loss for the year	–	–	–	(111.4)
Conversion of preference shares	58.9	–	–	–
Scrip dividends	(0.2)	–	–	2.6
Share options and long service awards	5.6	–	–	–
Transfers	–	(28.8)	(1.6)	30.4
At 31 December 1994	93.1	–	3.2	240.2

The special reserve was created in 1991 as a result of the cancellation of the share premium account, following increases in share capital and the share premium account this reserve is now distributable. Net exchange gains of £7.3m (1993 – losses £9.0m) arising on foreign currency net borrowings have been taken direct to reserves. The cumulative amount of goodwill, after merger relief of £116.0m and net of disposals, which has been charged to reserves is £135.7m (1993 – £275.0m).

Parent Company	Share premium £ million	Special reserve £ million	Other reserves £ million	Profit and loss account £ million
At 1 January 1994	28.8	28.8	2.6	227.9
Retained profit for the year	–	–	–	70.1
Conversion of preference shares	58.9	–	–	–
Scrip dividends	(0.2)	–	–	2.6
Share options and long service awards	5.6	–	–	–
Transfers	–	(28.8)	–	28.8
At 31 December 1994	93.1	–	2.6	329.4

In accordance with the exemption permitted by Section 230(3) of the Companies Act 1985, the parent company has not presented its own profit and loss account. The attributable profit for the year dealt with in the accounts of the parent company is £127.6m (1993 – £82.4m).

25 Cash flow statement

Reconciliation of operating profit to net cash flow from operating activities	1994 £ million	1993 £ million
Operating profit	**144.1**	163.8
Provision for rationalisation programme	**27.4**	–
Profits of associated undertakings, net of dividends	**–**	(0.9)
Profit on sale of associated undertakings	**(0.7)**	–
Depreciation and amortisation	**36.6**	36.0
Loss/(profit) on sale of tangible fixed assets	**0.3**	(3.2)
Restructuring costs	**(3.5)**	(6.8)
(Increase) in stocks	**(9.8)**	(10.7)
(Increase) in debtors	**(15.0)**	(10.7)
(Decrease)/increase in creditors and provisions	**(1.3)**	2.3
Net cash inflow from operating activities	**178.1**	169.8

Cash and cash equivalents

Balance of cash and cash equivalents		
Cash and bank	**135.0**	187.4
Bank loans and overdrafts	**(69.5)**	(192.4)
	65.5	(5.0)

Change in the balance of cash and cash equivalents		
Balance at 1 January 1994	**(5.0)**	76.4
Cash inflow/(outflow)	**62.9**	(72.7)
Exchange adjustments	**7.6**	(8.7)
Balance at 31 December 1994	**65.5**	(5.0)

Analysis of changes in financing	Share capital, premium and special reserve £ million	Convertible preferences shares £ million	Loans £ million	Total £ million
Balance at 1 January 1993	161.1	80.0	119.1	360.2
Cash inflows from financing	3.9	–	17.0	20.9
Transfer	(18.6)	–	–	(18.6)
Repayment of loans	–	–	(102.3)	(102.3)
Conversion of preference shares	14.8	(14.8)	–	–
Exchange adjustments	–	–	0.3	0.3
Balance at 31 December 1993	161.2	65.2	34.1	260.5
Cash inflows from financing	6.1	–	47.0	53.1
Transfer	(28.8)	–	–	(28.8)
Repayment of loans	–	(1.2)	(20.9)	(22.1)
Conversion of preference shares	64.0	(64.0)	–	–
Exchange adjustments	–	–	0.3	0.3
Balance at 31 December 1994	**202.5**	**–**	**60.5**	**263.0**

26 Financial commitments

Group capital expenditure contracted but not provided for in these accounts amounted to £4.5m (1993 – £6.1m). A further £28.6m (1993 – £16.9m) was authorised but contracts had not been entered into. The annual commitments of the Group under operating leases were as set out below:

	Land and buildings 1994 *£ million*	Land and buildings 1993 *£ million*	**Other assets 1994 *£ million***	Other assets 1993 *£ million*
Operating leases which expire:				
Within one year	**2.8**	0.9	**0.8**	1.3
Between one and five years	**1.7**	2.1	**3.5**	3.0
After five years	**2.8**	2.6	**–**	–
	7.3	5.6	**4.3**	4.3

27 Contingent liabilities

	Group 1994 *£ million*	Group 1993 *£ million*	**Parent 1994 *£ million***	Parent 1993 *£ million*
Guarantees in respect of subsidiary undertakings' borrowings	**–**	–	**41.4**	47.4
Other guarantees and contingent liabilities	**4.9**	4.7	**–**	–
	4.9	4.7	**41.4**	47.4

The Group is party to legal proceedings, in the normal course of business, which it is considered will not result in any material adverse effect on the Group.

28 Post-retirement benefits

The Group sponsors pension plans for its employees in most of the countries in which it has operating companies. In those countries where there is no company-sponsored pension plan, the state benefits are considered adequate. Employees' retirement benefits are the subject of regular review by management worldwide.

The Group's major pension plans are of the defined benefit type; the Group also operates defined contribution type plans as appropriate to local circumstances. Pension plans are established under the laws of the relevant territory with their assets held in separate trust funds or by insurance companies.

The pension cost for the Group's defined benefit plans has been determined by independent professionally qualified actuaries, using the projected unit credit method to give a substantially level percentage cost on the current and expected future pensionable payroll. The assumptions used vary according to local circumstances. The actuarial assumptions which have the greatest impact on pension costs are those in the United Kingdom and the USA, where the projected annual rate of investment return is 9.5% and 9.0%, and the projected annual increase in pensionable earnings is 6.5% and 6.0% respectively.

The Group's defined benefit plans provide retirement benefits for 59% of all Group employees. At the date of the most recent actuarial valuations (which took place between October 1992 and July 1994), the aggregate value of the assets of these plans was £182m, which represents an aggregate funding level of 124%. An amount of £6.2m (1993 – £5.8m) relating to the excess funding of Group pension schemes is included in debtors due after more than one year.

Costs of providing healthcare benefits after retirement of £0.5m (1993 – £0.6m) have been charged to operating profit. The accrued liability of £7.6m (1993 – £7.5m) is included in provisions.

principal subsidiary and associated undertakings

Principal subsidiary undertakings

The information provided below is given only for principal subsidiary undertakings in accordance with Section 231(5)(a) of the Companies Act 1985. A full list will be appended to the Company's next Annual Return.

At 31 December 1994	Activity	Countries of operation and incorporation or registration	% owned
United Kingdom			
Smith & Nephew Consumer Products Limited	Consumer	England and Wales	100%
Smith & Nephew Healthcare Limited	Healthcare	England and Wales	100%
Smith & Nephew Medical Limited	Healthcare	England and Wales	100%
Smith & Nephew Medical Fabrics Limited*	Healthcare	England and Wales	100%
Smith & Nephew Personal Hygiene Limited	Consumer	England and Wales	100%
Smith & Nephew Toiletries Limited	Consumer	England and Wales	100%
T. J. Smith & Nephew Limited	Healthcare	England and Wales	100%
Continental Europe			
Smith & Nephew SA-NV	Healthcare	Belgium	100%
Smith & Nephew A/S	Healthcare	Denmark	100%
Smith & Nephew Laboratoires Fisch SA	Healthcare	France	100%
Smith & Nephew Richards France SA	Healthcare	France	100%
Smith & Nephew Richards Medizintechnik GmbH	Healthcare	Germany	100%
BSN B Braun - Smith & Nephew GmbH	Healthcare	Germany	75%
Smith & Nephew Limited	Healthcare & Consumer	Ireland	100%
Smith & Nephew Srl	Healthcare	Italy	100%
Smith & Nephew Nederland BV	Healthcare	Netherlands	100%
Smith & Nephew AS	Healthcare	Norway	100%
Smith & Nephew Iberica SA	Healthcare	Spain	100%
Smith & Nephew Scandinavia AB	Healthcare	Sweden	100%
America			
Smith & Nephew Inc.	Healthcare	Canada	100%
Smith & Nephew Donjoy, Inc.	Healthcare	USA	100%
Smith & Nephew Dyonics, Inc.	Healthcare	USA	100%
Smith & Nephew Inc.	Healthcare	USA	100%
Smith & Nephew Richards, Inc	Healthcare	USA	100%
Smith & Nephew Rolyan, Inc.	Healthcare	USA	100%
Africa, Asia & Australasia			
Smith & Nephew Pty Limited*	Healthcare & Consumer	Australia	100%
Smith & Nephew (Far East) Limited*	Healthcare	Hong Kong	100%
Smith & Nephew Medical Limited	Healthcare	India	100%
Smith & Nephew KK	Healthcare	Japan	100%
Smith & Nephew (Sales) Sdn Berhad	Healthcare	Malaysia	100%
Smith & Nephew Limited	Healthcare & Consumer	New Zealand	100%
Smith & Nephew Pakistan (Pvt) Limited	Healthcare & Consumer	Pakistan	97%
Smith & Nephew Pte Limited	Healthcare	Singapore	100%
Smith & Nephew Limited	Healthcare & Consumer	South Africa	100%
Smith & Nephew Limited	Healthcare	Thailand	100%
Other			
Smith & Nephew Research Limited	Research	England and Wales	100%
Smith & Nephew Finance NV*	Finance	Netherlands Antilles	100%

*Owned directly by the parent company.

Principal associated undertakings

At 31 December 1994	Country of operation and incorporation or registration	Share capital *£ million*	Ordinary shares held
BSN B Braun - Smith & Nephew AG	Switzerland	0.5	50%
Eurociencia CA	Venezuela	0.4	49%
J L Morison (India) Limited*	India	0.3	28%
PT Central Sari Medical Supplies	Indonesia	0.4	50%

The activities of the above associated undertakings are the manufacture and sale of healthcare and consumer products and none has any debt securities attributable to the Company's interest.

group five year summary

Profit and loss account	1994 £ million	1993 £ million	1992 £ million	1991 £ million	1990 £ million
Turnover					
Continuing operations	**949.9**	899.4	780.6	697.3	621.3
Discontinued operations	**14.7**	49.3	77.1	94.4	108.4
	964.6	948.7	857.7	791.7	729.7
Operating profit					
Continuing operations:					
– before exceptional items	**172.9**	161.3	140.2	129.0	131.0
– rationalisation programme	**(27.4)**	–	–	–	–
Discontinued operations	**(1.4)**	2.5	3.5	4.8	8.4
	144.1	163.8	143.7	133.8	139.4
(Loss)/profit on disposals	**(150.3)**	7.3	(7.8)	(40.5)	6.5
Net profit on sale of Nivea trademark	–	–	40.1	–	–
Restructuring costs	–	–	(19.0)	–	(29.0)
Polteco settlement	–	–	–	(19.8)	(1.9)
(Loss)/profit before interest	**(6.2)**	171.1	157.0	73.5	115.0
Interest	**0.7**	(6.2)	(9.4)	(10.2)	(14.3)
(Loss)/profit before taxation	**(5.5)**	164.9	147.6	63.3	100.7
Taxation	**(48.4)**	(56.2)	(44.8)	(23.4)	(26.5)
(Loss)/profit after taxation	**(53.9)**	108.7	102.8	39.9	74.2
Ordinary dividends	**(57.5)**	(52.7)	(46.6)	(44.6)	(43.3)
Retained (loss)/profit	**(111.4)**	56.0	56.2	(4.7)	30.9
(Loss)/earnings per ordinary share	**(4.96)p**	10.55p	10.22p	3.99p	7.47p
Dividends per ordinary share	**5.28p**	4.91p	4.62p	4.44p	4.35p
Results before exceptional items					
Profit before taxation	**172.2**	157.6	134.3	123.6	125.1
Adjusted earnings per ordinary share	**10.62p**	10.15p	9.30p	8.86p	9.21p
Ratios					
Operating profit (before exceptional items) to sales of continuing operations	**18.2%**	17.9%	18.0%	18.5%	21.1%
Research and development to sales	**3.0%**	3.1%	2.8%	2.6%	2.3%
Capital expenditure to sales	**6.2%**	6.2%	5.9%	5.8%	5.8%

group five year summary

Balance Sheet	1994 £ million	1993 £ million	1992 £ million	1991 £ million	1990 £ million
Fixed assets – intangible assets	**8.8**	4.9	–	–	–
– tangible assets	**243.4**	241.7	242.3	219.5	209.1
– investments	**3.1**	5.6	3.0	2.0	6.7
Working capital	**233.2**	233.1	224.7	179.1	165.0
Provisions	**(47.6)**	(33.4)	(65.1)	(44.9)	(27.0)
Capital employed	**440.9**	451.9	404.9	355.7	353.8
Called-up share capital	**109.4**	103.6	102.0	100.6	99.9
Reserves	**336.5**	244.0	180.2	107.3	90.2
Capital and reserves	**445.9**	347.6	282.2	207.9	190.1
Net (cash)/borrowings	**(5.0)**	104.3	122.7	147.8	163.7
	440.9	451.9	404.9	355.7	353.8

Operating profit (before exceptional items) to average capital employed	**38%**	38%	38%	38%	37%
Gearing	–	30%	43%	71%	86%

Cash Flow					
Net cash inflow from operating activities	**178.1**	169.8	164.3	141.5	147.4
Capital investments net	**(55.8)**	(54.7)	(45.9)	(44.2)	(43.0)
	122.3	115.1	118.4	97.3	104.4
Interest, tax and dividends	**(103.2)**	(110.5)	(94.9)	(84.6)	(84.6)
Supplementary interest	–	(30.0)	–	–	–
Acquisitions and disposals	**12.8**	34.1	51.7	(5.8)	12.4
Polteco settlement	–	–	(19.2)	–	–
Issue of share capital	**6.1**	3.9	11.7	5.7	6.2
Net cash flow	**38.0**	12.6	67.7	12.6	38.4
Exchange adjustments	**7.3**	(9.0)	(42.6)	3.3	36.5
Conversion of preference shares	**64.0**	14.8	–	–	–
Opening net borrowings	**(104.3)**	(122.7)	(147.8)	(163.7)	(238.6)
Closing net cash/(borrowings)	**5.0**	(104.3)	(122.7)	(147.8)	(163.7)

information for shareholders

Analysis of shareholdings

Number of shareholders: 37,218 (as at 31 December 1994)

Shareholders range:	*Shareholders* %	*Shares* %
1,000 and under	25.33	0.44
1,001 to 5,000	50.38	4.43
5,001 to 10,000	13.24	3.22
10,001 to 100,000	8.96	7.37
Over 100,000	2.09	84.54

Held by :		
Banks	0.72	0.17
Insurance companies and pension funds	0.29	17.65
Nominee companies	16.75	63.37
Other corporate bodies	3.19	7.46
Individuals	79.05	11.35

Financial calendar	**1995**
Annual General Meeting	26 April
Payment of final dividend	4 July
Interim results announced	14 August
Payment of interim dividend	11 December
	1996
Full year results announced	early March
Annual Report posted	late March

Dividends The record date for this year's proposed final dividend, payable on 4 July 1995, is 19 May 1995. Shares will trade ex-dividend on the London Stock Exchange from 1 May 1995. Shareholders who wish their dividends to be paid directly to a bank or building society account should contact the Registrars at the address shown below. Shareholders may establish continuing mandates to receive ordinary shares instead of cash for their dividends. Details will be sent to shareholders in late May.

Low cost dealing service The Company has arranged a low cost dealing service in conjunction with Hoare Govett Corporate Finance Limited for private investors. Details may be obtained by writing to:
Hoare Govett Corporate Finance Limited
4 Broadgate
London EC2M 7LE.

Personal equity plans Henderson Financial Management Limited offers general and single company personal equity plans for UK residents wishing to hold Smith & Nephew shares in such plans. Further information may be obtained by writing to:
Henderson Financial Management Limited
3 Finsbury Avenue
London EC2M 2PA.

information for shareholders

UK capital gains tax For the purposes of capital gains tax the price of ordinary shares on 31 March 1982 was 28.67p.

Smith & Nephew share price The Company's share price is quoted daily in national newspapers as well as on Ceefax, page 222 and Teletext, page 514, where it is updated at intervals through the day. The Financial Times Cityline Service, telephone 0891 434043, will give an up to the minute share price. A fee is charged for this service.

Annual General Meeting The Company's 58th Annual General Meeting is to be held on 26 April 1995 at 11.00am at the Queen Elizabeth II Conference Centre, Broad Sanctuary, Westminster, London SW1. Notice of the meeting is enclosed with an accompanying letter from the Chairman.

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Solicitors: Ashurst Morris Crisp
Auditors: Ernst & Young
Stockbrokers: Cazenove & Co
Kleinwort Benson Securities

Reference
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