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### Net Interest Receivable/(Payable)

Interest income increased by £2.9m from £11.0m in 2003 to £13.9m in 2004. Interest expense decreased by £5.4m from £14.8m in 2003 to £9.4m in 2004. The Group's share of the joint venture's and associated undertaking's net interest expense was £1.4m and nil respectively compared with £1.5m and £0.7m respectively in 2003. Interest payable on currency swaps amounting to £14.6m was set off against interest receivable on swaps. Overall interest moved favourably by £9.1m from a net interest payable position of £6.0m to a net interest receivable position of £3.1m, due to favourable movements in interest and foreign exchange rates.

### Taxation

The taxation charge decreased by £29.3m to £52.7m in 2004. The taxation charge on profit before goodwill amortisation and exceptional items was £80.7m an increase of £10.5m on the 2003 charge due to higher profits. The effective rate of taxation on profit before goodwill amortisation and exceptional items was 29.0% the same as 2003. The taxation charge was reduced in 2004 by £28.0m as a consequence of the exceptional item and in 2003 increased by £11.8m as a result of the profit on disposal of the associated undertaking less exceptional costs.

### Business Segment Analysis

Group sales by business segment and geographic region and operating profit by business segment are set out below:

	2004	2003
	(£ million)	
<b>Sales by business segment</b>		
Orthopaedics	588.7	525.4
Endoscopy	304.8	300.0
Advanced wound management	355.0	353.5
Continuing Operations	1,248.5	1,178.9
<b>Operating profit by business segment</b>		
Orthopaedics	138.6	118.7
Endoscopy	61.8	59.5
Advanced wound management	51.1	42.5
Continuing Operations before goodwill amortisation and exceptional items	251.5	220.7
<b>Sales by geographic region</b>		
Europe (Continental Europe and United Kingdom)	409.7	369.9
United States	608.5	595.6
Africa, Asia and Australia and other America	230.3	213.4
Continuing Operations	1,248.5	1,178.9

### Orthopaedics

#### Sales

Orthopaedics sales were £588.7m in 2004, an increase of £63.3m or 12% compared to £525.4m for 2003. Underlying sales growth was 17%. Growth in sales in the US was 10% (22% underlying less 12% adverse currency translation). Outside the US, growth was 17% (10% underlying less 4% adverse currency translation and including 11% from the acquisition of MMT). Sales pricing in reconstruction and trauma increased by approximately 3% in the US.

In reconstruction, knee sales increased by 12% (21% underlying less 9% adverse currency translation). This comprised 12% in the US (24% underlying less 12% adverse currency translation), and 14% outside the US (16% underlying less 2% adverse currency translation). Hip sales increased globally by 21% (15% underlying less 10% adverse currency and including 16% from the acquisition of MMT), which included 2% growth in the US (14% underlying after 12% adverse currency translation), and 60% outside the US (17% underlying less 2% adverse currency translation plus 45% from the acquisition of MMT). This reflects continuing strong market conditions particularly in the US, the expansion of sales forces and the introduction of minimal incision surgery ("MIS") procedures.

Trauma benefited from the substantial investment in creating a dedicated US sales force, achieving a sales increase of 5% in the US, ahead of the market (17% underlying less adverse currency translation of 12%). Sales

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growth outside the US was 1% (4% underlying growth less 3% adverse currency translation). These result in 3% global growth (11% underlying less 8% adverse currency translation). Clinical Therapy sales, which consist of the SUPARTZ joint fluid therapy and EXOGEN ultrasound bone healing products, also benefited from sales force investment, growing 32% (44% underlying less 12% adverse currency translation) compared with last year.

A number of new orthopaedic products are in the pipeline. Marketing approval in the US for the ceramic on ceramic hip was received in December. Surgical evaluations for a new locking plate trauma product were started during the year and it is expected to launch this product in the first half of 2005. US pre-market approval application for the BHR product has been accepted for consideration by the FDA.

### **Operating Profit**

Operating profit from the orthopaedics business before goodwill amortisation and exceptional items increased by £19.9m (17%) from £118.7m in 2003 to £138.6m in 2004. The operating profit margin increased from 22.6% to 23.5% as a result of improvements to gross margin from cost and efficiency savings, partly offset by investment in sales force.

### **Endoscopy**

#### **Sales**

Endoscopy sales in 2004 were £304.8m, an increase of £4.8m or 2% compared to £300.0m for 2003. The underlying growth of 9%, represents a recovery from a problematic 2003. Sales in the US declined 3% (9% underlying growth less 12% adverse currency translation), but grew 7% outside the US (10% underlying less 3% adverse currency translation).

The new progressive scan camera system and the Group's comprehensive integration capability for digital operating rooms increased visualisation sales by 12% (22% underlying less 10% adverse currency translation). Repair product sales grew by 9% (underlying 16% less 7% adverse currency translation), led by the comprehensive range of shoulder products. Radio frequency sales were affected by an injunction imposed on US sales in connection with an ongoing patent dispute with a competitor, and declined by 12% (negative 2% underlying growth and 10% adverse currency translation) (see "Legal Proceedings"). Blade sales declined 3% (3% underlying growth less 6% adverse currency translation) following a stabilisation of the re-use of blades by US hospitals.

#### **Operating Profit**

Operating profit from the endoscopy business before goodwill amortisation and exceptional items increased by £2.3m (4%) from £59.5m in 2003 to £61.8m in 2004. The operating profit margin increased from 19.8% to 20.3% as a result of improved gross margins.

### **Advanced Wound Management**

#### **Sales**

Advanced wound management sales were £355.0m for 2004 largely unchanged from £353.5m in 2003. This is equivalent to 5% underlying growth less 5% adverse currency translation. Outside the US, sales grew 5% (8% underlying less 3% adverse currency translation). However, sales in the US declined 14% (negative 4% underlying growth and 10% adverse currency translation), where they were seriously affected by the need to switch to another enzyme debrider product. Loss of sales of the previous enzyme debrider negatively affected underlying global sales growth by 4%.

Globally, sales forces have refocused on the market opportunities for ALLEVYN hydrocellular dressings and ACTICOAT antimicrobial silver dressings. In the US, a targeted approach to DERMAGRAFT tissue engineered dermal replacement has been implemented. The benefits of this approach are evident in the sales of ALLEVYN, which grew 11% (15% underlying less 4% adverse currency translation), ACTICOAT, which grew by 38% (47% underlying less 9% adverse currency translation) and DERMAGRAFT, which grew by 16% (underlying 28% less 12% adverse currency translation).

#### **Operating Profit**

Operating profit from the advanced wound management business before goodwill amortisation and exceptional items increased by £8.6m (20%) from £42.5m in 2003 to £51.1m in 2004. The operating profit margin increased from 12.0% to 14.4% principally as a result of higher gross margins due to manufacturing efficiencies and expense control.

## 2003 YEAR

### Financial Highlights of 2003

Group turnover was £1,178.9m for the year ended 31 December 2003, representing 6% growth compared to 2002. Underlying growth in sales of continuing operations was 11%.

Profit on ordinary activities before taxation was £230.1m, compared with £177.9m in 2002. Profit before taxation goodwill amortisation and exceptional items (calculated as set out in the "Five Year Record"), improved 15% to £242.2m.

Basic earnings per Ordinary Share were 15.92p, a 31% increase compared to 12.11p for 2002. Adjusted basic earnings per Ordinary Share before goodwill amortisation and exceptional items (as set out in the "Five Year Record") were 18.49p compared to 16.02p for 2002, representing a 15% increase.

### Fiscal 2003 Compared with Fiscal 2002

The following table sets out certain profit and loss account data for the periods indicated:

	2003	2002
	(£ million)	
Group turnover (i)	1,178.9	1,109.9
Cost of sales	(345.1)	(329.9)
Gross profit	833.8	780.0
Marketing, selling and distribution	(440.1)	(414.1)
Administration	(125.5)	(127.1)
Research and development	(66.8)	(61.3)
BSN agency and management fees	19.3	20.6
Operating profit before goodwill amortisation and exceptional items (ii)	220.7	198.1
Amortisation of goodwill	(18.5)	(17.5)
Exceptional items	(22.4)	(29.9)
Group operating profit	179.8	150.7
Share of operating profit of joint venture: before exceptional items	22.7	19.6
Share of operating profit of joint venture: exceptional items	(2.7)	(2.6)
Share of operating profit of associated undertaking	4.8	4.9
Net profit on disposals	31.5	18.0
Profit on ordinary activities before interest	236.1	190.6
Net interest payable	(6.0)	(12.7)
Profit on ordinary activities before taxation	230.1	177.9
Taxation	(82.0)	(65.8)
Attributable profit for the year	148.1	112.1

(i) Group turnover comprised £1,178.9m from Continuing Operations (2002 – £1,083.7m from Continuing Operations and £26.2m from discontinued operations).

(ii) Operating profit before goodwill amortisation and exceptional items comprised £220.7m from Continuing Operations (2002 – £196.0m from Continuing Operations and £2.1m from discontinued operations).

### Group Turnover

For the year ended 31 December 2003, group turnover totalled £1,178.9m, an increase of 6% or £69.0m compared to £1,109.9m for 2002. Underlying growth of Continuing Operations was 11%. Translation of foreign currencies had the effect of decreasing turnover by 2%, primarily due to the depreciation of the US Dollar against Sterling. The loss of revenues from the Group's discontinued rehabilitation business resulted in an adverse impact to the Group's turnover of £26.2m (3%). Selling price increases accounted for approximately 2% of the underlying sales growth.

### Cost of Sales

Cost of sales at £345.1m represented 29.3% of sales compared to 29.7% in 2002. This improvement arose from manufacturing cost and efficiency savings and transactional currency benefits from the decline in the value of the US Dollar reducing the product cost in many countries outside the US, notably in Europe and Australia. The reduction in cost of sales would have been greater but for the acquisition, in late 2002, of the remaining DERMAGRAFT interests not already owned which increased the Group's production costs for this product.