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PRESENTATION

David Illingworth - *Smith & Nephew - Chief Executive*

Well, good morning everyone. Welcome to our second quarter results presentation. The Safe Harbor statement was just being read to our online participants. I'll reference the Safe Harbor statement in your booklet for all of you attending live. I'm Dave Illingworth. I'm going to briefly talk about the business and some wide areas of interest, and then Adrian is going to take you through the numbers.

The second quarter has been a solid quarter for us as the actions we've taken to improve our performance are delivering benefits. Now this quarter was the first $1b quarter for Smith & Nephew in our 152-year history. Clearly, a milestone worth noting, and we're pleased to have delivered across all of our businesses.

In Reconstruction, both Hips and Knees performed well. The changes we made in Trauma have improved revenues in the US. Endoscopy has delivered double-digit growth and Advanced Wound Management has exceeded market growth globally. And Negative Pressure Wound Therapy continues to gain traction.

We're investing in our business for the future. It's part of our strategy and we're going to continue to invest in our business to sustain our profitable growth in the second half.

Before I talk about the business in detail, I just want to mention and discuss Plus briefly.

Firstly, our investigation into the sales practice issues is largely complete and we continue to believe that $100m is the right number for our lost revenues in a full 12-month period. The legal processes are started and the indications are that it will be -- it could be two to three years before we have an outcome. Meanwhile, though, management is focused on getting the benefits from this acquisition.

Our market positions in the Reconstruction and Trauma businesses in Europe have been stabilized and we've seen some good outcomes. For example, improved revenues of JOURNEY and DEUCE in Germany, as well as the cross-selling of our combined products beginning to take hold.

We've also combined some research in development projects to get the best efficiency and effectiveness out of our efforts. The cost synergies that we're getting include head office, sales and marketing, distribution and administration. Our European business now is operating as one Company in Europe, and that's important. It's headquartered in Rotkreuz, Switzerland, and we're beginning to see the benefits from this acquisition.

Let me move on and talk a little bit about the market conditions.

How do we see the environment at the moment? Well, this chart really speaks to the historic resilience of our markets. And we continue to see demographics driving procedural volumes in our business. We see, as we always have done, pricing pressures in some markets, and in these markets we find that innovation is rewarded where there is quantifiable economic and clinical value. We have also seen some inflationary pressures and, so far, these pressures have been manageable.

Now, moving on to look at our Group strategy for our markets.

Now I know there may appear to be a lot on this slide, but it emphasizes our core strategy and how we are increasing the links between our businesses. Not just in the centralization and procurement and other back office systems, but the sharing of best practices in manufacturing, sales, marketing and outsourcing. We have consistent strategies across our business units.

Our growth strategy is unchanged. We are in the business to help people live healthier, more active lives and we deliver sustainable, profitable growth. And we have a clear strategy to make this happen. There are four key components of our strategy.

First, customer-focused product innovation to drive growth in the fast-growing segments. Secondly, Earnings Improvement Program to deliver improved profitability. Third, to strengthen our market positions through internal growth and value enhancing acquisitions. And, fourth, to have a strong balance sheet and cash flow so that we can make the investments required.

I'm now going to look at each of the businesses in turn, starting with Reconstruction.

Q2 was a good quarter with a strong contribution from both Hips and Knees, with revenue growth of 11%, excluding the Plus impact. And with that 11% growth we exceeded the market rate -- growth rate again this quarter.

Our Hip franchise had a very good quarter across the business. BHR now has about 3.5% of the US market by volume; a very good achievement in its second year in the market. And we're clearly pleased with our progress. This quarter saw a slowing of the growth rate against very tough comparators.

In the same quarter last year, US Hips grew by 50%; the best performance in Smith & Nephew's history. We see nothing that tells us that RESURFACING in the US will be any different to any place else. And we see nothing that suggests that we won't have at least a majority share of that market.

Knee revenue growth, 9% in the quarter, was driven by increased market penetration by our JOURNEY system. Also in Europe, we have seen our revenues strengthening as a result of the Plus acquisition, and as those related issues have eased. Margin improvement in Reconstruction was 170 basis points in the quarter and was driven primarily by our Earnings Improvement Program.

Now looking forward for the rest of the year, the Reconstruction market is performing well and we see continued good performance for the rest of the year. We expect to see continued benefits from Plus coming through in Europe as our cross-selling actions continue to pay off.

We've been strengthening our brand awareness and we expect to see benefits from this this year as well. I would ask all of you and, in fact, I'd encourage all of you to look at our new advertising campaign, a sample of it at least, and the link is on this slide. We have some great new products. We have approval of OXINIUM in Japan. We have new sizes for BHR available and JOURNEY is doing very well.

I'd like to talk just briefly about the JOURNEY family of products, which are a big growth driver for us right at the moment. JOURNEY is focused on the younger, more active patient segment that we are targeting. 32 surgeons have worked on the JOURNEY family for seven years now. The family started as one product and has grown to the range of products you see on this slide.

The patient benefits with JOURNEY are significant. They get a better outcome, more mobility and a more natural gait after surgery. JOURNEY can be used to treat only the disease-affected part of the joint, preserving healthy tissue and bone, leaving options for later treatments.

The design of instrument sets is as much a part of the process as the design of the product. JOURNEY's instruments have been designed for efficiency and ease of use. And the standardization of instruments across the family allows surgeons to easily use the whole range of JOURNEY products. For the hospital, they get a higher-tech product which attracts a different mix of patients, increasing their attraction in the marketplace.

Turning to Trauma and Clinical Therapies. It's a little early to claim victory on this from the changes we made, but we are seeing clear signs of progress as we now have the US sales organization under one sales management team. Our dedicated Trauma sales force and our full line reps in the US who sell both Reconstruction and Trauma products, have stepped up to the plate and performed much better this quarter.

US Fixation revenues grew at 4%. We took the actions that we needed to, and now we're focused on getting back to the growth rates that we know a strong, customer-focused approach can deliver. And also note that Clinical Therapies benefited from excellent growth in EXOGEN revenues of 26% this quarter.

Growth for Trauma in the second half will be driven by procedural volumes and our investments in training, sales programs and instrument sets. We also expect synergies from Plus to make a contribution. Going forward for Trauma, it's all about getting on with what know is right. We believe the structure is sound, we have great products, we have the right plans and systems in place and we do expect synergies from Plus to contribute to growth as it expands our coverage in Europe.

So, turning to Endoscopy. Endoscopy had a good quarter, returning to double-digit revenue growth driven by growth in our Knee business, particularly with FAST-FIX and ENDOBUTTON. And in Shoulders, driven by BIORAPTOR and TWINFIX. Our US business improved its revenues by 7% over the previous quarter, with a 4% growth rate as the changes made in this business began to be productive.

Outside the US, Endoscopy continues to perform extremely well, posting a growth of 16%, which we believe is well above the market rate.

And, looking to the second half for Endoscopy, it looks like this. First of all, we're still -- we are the global leader in arthroscopy and sports medicine. It's a position built from our US strength.

Outside the US we see many opportunities to continue our strong momentum driving further penetration and growth. We're constantly innovating, developing new products, such as the FOOTPRINT PK Suture Anchor launched at AANA this year. This FOOTPRINT Anchor incorporates a unique design that enables surgeons to apply precisely the desired amount of suture tendon -- tension.

We expect, in the second half, our business outside the US will continue to perform well. And, as we've outlined before, we expect it will take several quarters before our US business is where we want it to be.

And moving on to Advanced Wound Management, we've achieved a number of improvements this quarter. Firstly, the business outside the US, which is about 80% of the total, grew at 10%, out-pacing the estimated market growth of 8%.

Secondly, in the US, Advanced Wound Care products returned to growth and grew by 3%. And this adds up to a 9% global revenue growth, which we also believe outperformed the global market growth rate in the quarter.

Thirdly, our investments in Negative Pressure Wound Therapy, or NPWT, have started to pay off as we have won accounts in all three of the market segments; acute care, long-term care and home care.

It's still early days for our Negative Pressure Wound Therapy products in our business but we are calmly confident about our ability to compete and, ultimately, lead this fast-growing segment. Let me give you a little more insight into why we are confident.

I recently spent some time with Gary Blackford. I don't know if you all know him, but he's Chairman and CEO of Universal Hospital Services, UHS; it's the leading national medical equipment outsourcing company. And I'll tell you what he told me. And I quote, "We have seen a tremendous response from customers to the Smith & Nephew Negative Pressure Wound Therapy products. We see dozens of new product introductions in our equipment portfolio every year and the reception to the Smith & Nephew product is one of the best I have ever seen at UHS."

We're very committed to this market and to continuing our investment so that we will build a world-class business. So in the second half of the year it looks promising. Our Advanced Wound Care products like ALLEVYN GENTLE BORDER and ALLEVYN Ag are driving growth in our Dressings and Infection Management segment. In Negative Pressure Wound Therapy, our products are launched in all the major markets and we're billing over 500 accounts.

Our investments in training and evaluations are turning into customer usage. We have 50 new sales reps now in their second six months and showing productivity. We've also seen the efficacy of our products endorsed by academic papers, including Lund University of Sweden's presentation at the World Congress in Toronto, and we've won accounts with major hospitals in the US. And our products have been listed by healthcare systems in the US, Europe and Australia.

Now let me turn to the Earnings Improvement Program. EIP is a very important pillar of our growth strategy, and this gives you some of the things that we have done so far. We have 26 major initiatives with 10 complete, the others active, and new items coming on line. This Program has everything to do with operating more efficiently, effectively and profitably and can be broadly categorized as manufacturing costs of goods, portfolio, infrastructure and sales and operational excellence.

The Program is not just about cost, although there are clearly elements of that. But the emphasis is on use of resources. Our employees and our customers know our focus is on how we can do it better, faster and more effectively and free up resources to invest in what is important versus what does not add value. We want these initiatives to drive both the top and the bottom line in our business. The focus is delivering well for us and we expect it to continue to do so.

So, EIP in process. I want to give you an indication of some of the current and future projects which we're working on, and illustrate how we are in the classic mid-Program heavy lifting phase as I call it. I won't go through all of this, but just to give you some color on the projects, here are some examples of what we're doing.

Last month, the Executive team, including myself, held the groundbreaking ceremony in China for a major new manufacturing facility. We have a new distribution center in Baar, Switzerland, which will become fully operational this year. Jeff Adams, our new Head of Global Operation is bringing world-class procurement, lean manufacturing and process re-engineering skills into effect across our business.

You can see that, increasingly, the business units are working together on joint projects to give us Group-wide operational leverage. This Program, like I said, is not just about cost cutting. It's about growing both the top and bottom lines of our business. We are now two years into the Program and hitting it hard with lots of activity.

I'm now going to hand it over to Adrian to take you through the numbers. Adrian.

Adrian Hennah - *Smith & Nephew - CFO*

Thank you, sir. Well, thank you, Dave. And, good afternoon, ladies and gentlemen. If we could now turn to slide 19, which is the income statement.

Revenue in the quarter was $1b, giving us a headline growth of 23% on the comparable period last year. Underlying growth, after adjusting for exchange rates and for the acquisition of Plus and BlueSky, was 8%. Excluding the impact of Plus sales loss due to changes to unacceptable business practices, Group sales grew at constant currency by 10%.

We estimate that sales of $19m were lost in the quarter, $11m in Recon and $8m in Trauma. We estimate that the overall Group growth number was increased by about 1% due to the higher number of selling days in quarter two; 64 as compared to 63 last year.

Trading profit in the quarter was $198m, representing an underlying growth of 8%. The underlying increase in the trading margin was five basis points in the quarter. We estimate that trading profit was reduced by about $9m as a result of the lost Plus sales and related costs. But for this Plus effect, underlying Q2 trading margin would have grown by 60 basis points.

The amortization charge for acquisition intangibles in the quarter, $7m, includes a minor true-up as the acquisition balance sheet values for Plus were finalized one year after acquisition, as required under IFRS 3. On an ongoing basis, we expect an amortization charge for acquisition intangibles of $10m a quarter, including $6m in respect of Plus and BlueSky.

Moving to slide 20, and further down the income statement, the tax charge in quarter two, before exceptionals and amortization, is 31%; our expected rate for the full year. Adjusted attributable profit for quarter two was $125m. Adjusted earnings per share grew at 13%. This is higher than underlying trading profit growth of 8%, as exchange movements increased earnings by about 3% and accretion on the share buyback increased it by a further about 1%.

So if we could then turn to the next slide, slide 21, and an analysis of revenue by business segment. You've heard from Dave on the progress of each business. On this schedule you can see the growth rates in the quarter, to which Dave referred, for each of our business segments.

We've shown pro forma growth rates, excluding the impact of the changes to Plus sales practices, at the right-hand side of this table. Pro forma underlying sales growth was 10% for the Group as a whole. As we've mentioned, it was 11% for Recon and 10% for Trauma.

Turning to the next slide, slide 22, and an analysis of revenue growth rates by segment and by geography. The underlying growth rate in our Reconstruction business was 8%. Hips grew at 7%, Knees at 9%.

In the United States, growth in the Knee business was 12%, with good growth from the newer products. Hip growth in the US was 7%.

In Europe, underlying Recon sales growth was 3%. And, adjusting on a pro forma basis for the $11m sales practice effect, Recon achieved a sales growth in Europe of 11%.

Like-for-like overall pricing in our Reconstruction business in the USA, and outside the USA, was slightly negative.

The Trauma and Clinical Therapies growth rate was 5% before adjustment for the sales practices effect. Growth in Fixation was 4% in the USA. We continue to expect to see significant improvement as the new US field sales force arrangements gain traction. Clinical Therapy sales growth was 6%.

In Europe, Trauma and CT sales fell by 12%. They grew by 9% after adjusting for the $8m of sales practices effect.

Endoscopy growth rate was 10%. Within this, the Arthroscopy growth rate was 10% and Visualization sales rose by 12%. Endo sales outside the USA were again strong with double-digit growth, and sales grew in the USA by 4%.

Wound sales grew at 9%. NPWT sales are, as expected, contributing only modestly at this stage to growth. Total Wound sales grew 3% in the USA, 9% in Europe and 10% in the rest of the world. Sales growth in the USA, excluding NPWT, was broadly flat, again impacted by the sales force focus on NPWT. But, as expected, significantly less impacted than in quarter one.

Turning to the next slide, slide 23, this shows the usual analysis of revenue and trading profit by business segment. As we've already noted, underlying trading margin for the Group overall increased in the quarter by five basis points. The reported margin decline of 70 basis points was diluted by consolidating the lower margin Plus sales which we acquired, as you know, during quarter two last year. As noted earlier, the underlying increase in the Group trading margin would have been about 60 basis points but for the changes to Plus sales practices.

Recon showed strong underlying margin improvement in the quarter of 170 basis points, even after the impact of the Plus changes and bearing the cost to the monitor and associated expenses under the Deferred Prosecution Agreement in the USA.

The Trauma margin was impacted by the Plus changes. Endo margin was impacted by costs associated with the Arthrex court case and some business development activity. We have not booked any gains from the court award of $15m against Arthrex as there could still be an appeal. We have, however, booked significant legal costs.

Margin in Wound was, as expected, lower, due to investment in our new NPWT products. Excluding NPWT, the margin would have been close to the comparative quarter. NPWT was again loss making in quarter two, though less so than in quarter one.

Turning then to slide 24, and the outlook for the rest of 2008. Our view of the Company's overall outlook is unchanged from quarter one. We continue to expect the sales practice changes in Plus to reduce revenues in a full 12-month period by about $100m, and the impact on 2008 revenues to be somewhat lower than this.

We continue to expect that the impact on profit of the lost sales, after initial transition, will be the trading profit margin in Recon and Trauma, i.e., around 25%. We are seeing a somewhat higher impact on profit and margin in the short term, about $9m profit impact on $19m sales in quarter two, or 47%. We expect this percent to fall significantly over the next several quarters into next year as we remove unnecessary overheads and incur fewer professional advisor fees.

In the Orthopedic Implant area, we believe that underlying global market growth remained about 8% through quarter two. We continue to expect our growth to exceed market growth in the USA in 2008. We continue to expect that the growth in Europe will be reduced by the impact of the Plus changes.

Within Orthopedic Fixation, we have seen global market growth down slightly to about 10% in quarter two, with a modest reduction in the USA and no change outside the USA. In the USA, we continue to expect to recover to market growth in Fixation by the year end. We continue to expect that the growth in Europe will be reduced by the impact of the Plus changes.

For Endo and Wound, our view of the market growth and of our sales performance in 2008 remains the same as in May and, indeed, in February.

As far as margins are concerned, we continue to expect a short-term impact on margins from the Plus sales practice changes and the NPWT launch. We expect the loss of profit on lost Plus sales, as we mentioned, to reduce to 25% of the lost sales during the first half of 2009.

We do not expect our NPWT sales to earn material profit for a few quarters as we invest in substantial potential of our current and pipeline NPWT products. We expect them to be substantially profitable thereafter.

We remain firmly on track with our Earnings Improvement Program. As you know, we are combining the management of our Recon and Trauma sales forces in order to improve service levels to customers and also the management of the Recon and Trauma support functions. These changes have now been implemented.

From next quarter, we will therefore be adjusting our segmental reporting to reflect this revised business unit structure. We will be reporting the results of the previous Recon and Trauma business units in a single Ortho business unit. We will therefore report three segments; Ortho, Endo and Wound. In order to continue to assist your understanding of the business we will continue to supply sales data for Knees, Hips, Fixation and Clinical Therapies, as we do now.

And with that update on the outlook, I'll hand back to Dave.

David Illingworth - *Smith & Nephew - Chief Executive*

Thank you. Thank you, Adrian. The -- before we take questions, and after a lot of detail from Adrian's -- Adrian about the quarter, I just want to remind you all about our strategy for growth in the medium term.

Our growth strategy is to deliver customer-focused product innovation to drive growth in fast-growing segments, one. Secondly, to use our Earnings Improvement Program to deliver improved profitability, to strengthen our market positions through internal growth and value enhancing acquisitions and to use a strong balance sheet and cash flow to enable investment.

We see a great future for our business based on our market, our products and our people.

And, with that, I will turn it back to the moderator for questions. We'll use the -- our usual system of sharing questions from the audiences here in London and also with our conference call audience from both sides of the Atlantic.

We will take two questions from people here in London and then take a couple of questions from our conference call audience. Can each person please limit their number of questions to two or three at most, to allow as many people as possible to the opportunity to participate?

And can we have our first questions from the floor, please?

QUESTIONS AND ANSWERS

David Illingworth - *Smith & Nephew - Chief Executive*

Peter.

Peter Cartwright - *Evolution Securities - Analyst*

Peter Cartwright, Evolution Securities. Could you just say again what you think the impact of the problems at Plus will be in 2009? And is that any change to what you thought a quarter ago, the fact that it's rolling into 2009?

David Illingworth - *Smith & Nephew - Chief Executive*

Do you want to start off with that?

Adrian Hennah - *Smith & Nephew - CFO*

Sure. There's absolutely no change from what we said a quarter ago. We believe the position as we saw it then is exactly the position as we see it now. And, to repeat, we believe in a full year lost sales are $100m. And we believe in a full year the drop through will be 25%, so $25m lost profit. We expect to get to that drop through at 25% in the early part of 2009. So you might find it's marginally more than that on the profit effect in 2009, but certainly close to it. Does that make sense? I thought it did.

David Illingworth - *Smith & Nephew - Chief Executive*

Charles.

Charles Weston - *Nomura Code Securities Ltd. - Analyst*

Hello. Charles Weston from Nomura Code. I'll take three questions, please. The first, just to get your comments really on the prospects for the elective procedures in the US. There have been some analyses out there showing that elective procedures have been delayed or postponed because of high co-pays, but you don't seem to be seeing any of that, given your comments earlier today. So I was wondering if you could perhaps talk around that a little bit.

Secondly, on the margins in the Trauma business, I understand that you've been changing round the structure of the sales force there. But if you could elaborate on how you spent more in the near term and how you see that panning out in the longer term, that would be helpful.

And, lastly, on your plant in China, what is it that you intend to manufacture in China in the 2010 and beyond?

David Illingworth - *Smith & Nephew - Chief Executive*

Okay, great. Thanks for those. I'll start with the elective procedures. I'm not sure I can add a lot to your insightful analysis of it and the other analysts in the room. I read the -- I read your reports. We haven't seen a big impact on this as of yet. We still see the procedural volumes as strong. We --- our business in the Reconstructive part of our Orthopedic business is doing well. We did see a slowing of BHR in the quarter, as we talked about, mainly due to comparables being pretty tough [of] 50% of a year earlier.

So we're not feeling it quite as much, but we're certainly keeping an eye on it, and really I don't have a lot to add in that regard.

In terms of our Trauma business, I appreciate the question because, quite frankly, we didn't do a very good job of communicating this last quarter exactly what we were doing. As you know, I used to be the President of the Orthopedics business so I know that business pretty intimately. And we've been working on divisionalization of our Trauma and our Reconstructive businesses for over five years, for as long as I'd been there.

My vision has been to have very unique customer front ends and sales channels that can really relate to those specific surgeons where it makes sense. And we did that in the US and got some great results as a result of it. We also needed to make sure that we had a full complement of products and we're putting a lot of focus on the Trauma business. And, quite frankly, I think we went a little too far. We completely divisionalized it, a hard divisionalization including management, not just sales forces. And what we found was that we got less collaboration between the sales channels and that collaboration turned out to be important.

So we -- I was pretty convinced, mainly because I have an intimate knowledge of close and close up -- up close and personal knowledge of that business and the dynamics of it. I was pretty convinced that if we fixed the sales management issue in that business that we would see it start to come back to where we wanted it to be. And it's too early to claim complete victory on that, Charles. I'm not even going to try. But we've seen -- we're seeing the cooperation now and we're seeing the right things and the right behaviors. And I'm absolutely convinced it was the right move. And we fully expect to get that business back to market growth rates by the end of the year.

If you want -- was there another part of that question on Trauma?

Adrian Hennah - *Smith & Nephew - CFO*

I think there was a question on margins tied to it. Yes, the -- there is no increase in cost of putting these two together. There's in fact a decrease in cost. It's one of the -- it's a side benefit of putting the managements back together in the way Dave described.

Behind that, you may say, well, there of course -- why are Trauma margins not higher in the quarter? There's two reasons for that. One is, as you'll have seen, a significant part of the shortfall for Plus or Plus sales practice sales is in Trauma. In fact, $8m of the $19m is in Trauma. And, although we're not splitting the profit, the lost profit of $9m, a significant amount of that is in Trauma, so Trauma has been quite badly hit by this.

And, secondly, it's warf and weft. We cannot say often enough; you can't over-read quarterly movements by segment because you'll fool yourself if you do. So there's nothing significant in that.

David Illingworth - *Smith & Nephew - Chief Executive*

Yes, and I think the last part of maybe over-answering this rich question that you asked --

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Charles Weston - *Nomura Code Securities Ltd. - Analyst*

Yes.

David Illingworth - *Smith & Nephew - Chief Executive*

-- is that there -- totally unrelated, we have started on a process where we are centralizing some of the non-customer facing activities in our businesses. So we're centralizing operations and centralizing IT and procurement and all those other things. So it just made -- it was not related to what we had done earlier but it was very compatible to getting those businesses back under a common management structure, because it makes it easier for us to get that centralization of operations.

There's no reason why we have to have a manufacturing facility for Trauma and a manufacturing facility for Recon. We can share those facilities. It doesn't make any sense to do that. So I think that's the last piece of that -- of that one.

On China, the -- we actually have two facilities that we're building in China. One is going to be for our Orthopedic business. And the other that I referred to was the groundbreaking for our Wound, Advanced Wound Care business. We've already announced the closure of our Largo, Florida plant and we're transferring all of that manufacturing -- substantially all of that manufacturing, over to China. We're also taking some other manufacturing in different parts of the world for Wound Care as well and moving it to that facility as well.

It's going to serve two purposes for us. It really is a two-pronged strategy that may not seem to be totally related. One is a lower cost manufacturing base. And that's clear. That's easy to calculate. And we'll have some gauze-based products and bone-based products and different types of things that we're going to be manufacturing at that facility.

The other thing is that if you're going to establish a lower cost manufacturing base, why not do it in the country that everybody believes is going to have a tremendous impact and tremendous potential in two years, three years, five years, 10 years; pick the timeframe?

So our feeling was, strategically, why not go to the lower cost manufacturing in a country that would give us a critical mass and a base of operations so that we could get real people on the ground, start developing relationships with customers and government officials and all the other things, so that we could exploit the Chinese market when it became commercially available to us. And that's just as transparent as I could be on our strategy for that.

Charles Weston - *Nomura Code Securities Ltd. - Analyst*

Thank you.

David Illingworth - *Smith & Nephew - Chief Executive*

You're welcome. I think we'll take two questions from the Internet, or the Web, or the phone lines, or wherever these folks are.

Operator

Thank you. We'll take our first question from Matt Miksic of Piper Jaffray. Please go ahead.

Matt Miksic - *Piper Jaffray & Co. - Analyst*

Hi. Can you hear me okay?

David Illingworth - *Smith & Nephew - Chief Executive*

Yes.

Matt Miksic - *Piper Jaffray & Co. - Analyst*

Thanks for taking the question. You talked a little bit about in your Earnings Improvement Program the -- using your resources differently and more efficiently. I was wondering if you could talk a little about what you're doing there, in particular in sales and distribution.

David Illingworth - *Smith & Nephew - Chief Executive*

Well, let me see what I -- I'll see what I can do to focus in on sales and distribution. But let me give you the vision, and why we state it that way that it's not just about cost cutting.

In order to accomplish what we want to accomplish we need real cultural change within our Organization. We want to take our 152 years of history and take the good parts and make the cultural changes and do the things differently that we need to do to be more productive in the future. That's this over-arching vision.

It's really hard to get people engaged about cost-cutting activities. People have a hard time figuring out how they can save their way to prosperity. A lot of folks in our Organization want to grow their way to prosperity. So the way that we've -- the deal that we've struck and the way that we're getting real substantive engagement of our people and our businesses is we're saying, look, this is about taking all of that non-productive stuff that we're currently doing through inefficiency and figuring out a way to give some back to the shareholders and keep some in the other hand to -- for additional investment.

We'll make investments in those fast-growing market segments, like Negative Pressure or the active and -- the younger, more active, informed patient. And that's how we're getting people motivated and excited about what we're doing.

In terms of sales specifically, it was a fairly mechanical exercise where we -- where we went and looked at the actual productivity of our sales channels by territory, the way they were deployed, the fact that we had multiple sales channels. And we essentially went and made some corrections, changed some boundaries and did some things differently on the sales deployment side, and we actually saved a chunk of money as a result of it.

Matt Miksic - *Piper Jaffray & Co. - Analyst*

Okay. And any -- does any of that, either in -- on the Negative Pressure Wound Therapy side or in the Recon side involve building out in your sales force as well?

David Illingworth - *Smith & Nephew - Chief Executive*

Well, yes, it does. We're committed to unique sales channels. We have our Clinical sales channel which is -- we've created in my lifetime here in the last five or six years. And now it's a world-class sales channel. We've built that out. We've built out the Trauma independent sales force. It -- that was zero in my lifetime here with the Company. And the reason I say it that way, it's in recent memory. These are recent things that have happened.

So we continually look at how we can -- and I think the jury is still out a little bit on exactly what the model is going to be on Negative Pressure. I mean we're learning as we go. We have a precedent model in the marketplace that we have to react to. There's just no other way to do it.

When you have a monopoly player in a very large market, and very entrenched, they can, for at least a period of time, dictate the terms of what the business model needs to look like and the sales model needs to look like. So we're reacting to that. We would hope to get to the point in the future that we can start determining what the future looks like in terms of deployment of resources there.

Matt Miksic - *Piper Jaffray & Co. - Analyst*

And just thinking specifically, any adds in the Recon business in the sales profit?

David Illingworth - *Smith & Nephew - Chief Executive*

Yes. Yes, we're still adding people is the answer to that.

Matt Miksic - *Piper Jaffray & Co. - Analyst*

Can I ask just one follow up to Adrian here on the tax rate? I guess we saw a number that was a little bigger than we were expecting. Could you talk -- if you could just talk a little bit about the trends in the tax rate and what we can expect going forward.

Adrian Hennah - *Smith & Nephew - CFO*

Well, I think the tax rate was 31.4 or something, 31, it's certainly round at the 31%, which has been our expectation for the year and our guidance for the year since the end of last year. So I'm -- we weren't surprised by the tax rate, let me put it that way.

Looking forward, there are pressures both ways. There are, as we've identified before, the -- at 31% we're less than our natural rate which, if you balance the rate of the countries in which we operate, it would come in at sort of 35%, 36%. So you've got to continually work to get that number down, which we are doing. So, therefore, you're battling against slight upward pressures, which we've signaled. And we have signaled maybe a very modest increase in the tax rate over the next years, but it will only be modest and not significant in our view.

Matt Miksic - *Piper Jaffray & Co. - Analyst*

Great. Thank you.

David Illingworth - *Smith & Nephew - Chief Executive*

Thank you very much. Next question.

Operator

Thank you. We'll take our next question from Michael Jungling of Merrill Lynch. Please go ahead.

Michael Jungling - *Merrill Lynch - Analyst*

Thank you. I've got three questions, please. Firstly, on the Earnings Improvement Program, can you split out what the underlying margin benefit has been in Q1 and Q2 for 2008, if you exclude Plus and you exclude Negative Pressure Wound Therapy and perhaps some of the legal costs that you're incurring for the issues that you've got with Plus? I'm finding it a little bit difficult to track.

Secondly, in the past you've disclosed this is in your presentation, so could you give us the constant currency growth for Hips and Knees, US and outside the US? I think you've mentioned some on the call, but also sales, excluding Plus, for Hips and Knees in the US and outside the US.

And then the third question on Fixation, you mentioned that the US market has slowed down and it seems that this is indeed true. I'm just curious why you think the US Trauma market is slowing down? and perhaps maybe it's driven by lower car accidents because of less miles traveled? That would be great, thank you.

David Illingworth - *Smith & Nephew - Chief Executive*

Okay, Adrian.

Adrian Hennah - *Smith & Nephew - CFO*

Yes, well that first question was a 'Junglingism'. The -- Michael, I'm actually not quite sure how to answer that first question. There's various bits of data we put in the presentation. Why don't you give me a call afterwards and we can zero in on exactly which one you're most interested in? I think I'm going to baffle everyone with numbers if I try and respond to the full breadth of that.

But certainly your question on Hips and Knees, US, outside US, happy to run through those slowly now.

Our -- if we start with Hips, we had a global growth of 7% which was also a US growth of 7% and an outside US growth of 7%, so that one was fairly simple. Knees, a global growth of 9%, comprising a US growth of 12% and an OUS of 8%, which means for total Recon we had an 8% growth, 9% in the US and 7% outside the US. And for Fixation we reported 4% for the Group overall, which was 4% in the US and 3% outside the US.

I hope that at least answers your second question.

Michael Jungling - *Merrill Lynch - Analyst*

And sales as well, Adrian?

Adrian Hennah - *Smith & Nephew - CFO*

Excuse me?

Michael Jungling - *Merrill Lynch - Analyst*

Can you also mention the sales that you have in those US, outside the US?

Adrian Hennah - *Smith & Nephew - CFO*

Well, they're in the presentation, Michael. We give a geographic analysis. All you've got to do is to -- no, not Hips and Knees. No. Well, let me come --- hold on, have I got that here? Why don't you answer the last bit while I look this one up?

David Illingworth - *Smith & Nephew - Chief Executive*

You're going to give me the piece on car accidents?

Adrian Hennah - *Smith & Nephew - CFO*

Yes, car accidents. Well, he's written about it in his report so we know the answer.

David Illingworth - *Smith & Nephew - Chief Executive*

I think you know more -- I think this goes back to the answer I gave Charles. I think you know more about it than I do, Michael. We -- I -- it's hard for us to understand the pluses and minuses by quarter in some of these markets. I think we're going to keep the -- keep following it and trying to understand it, but we -- it's softens somewhat and we're going to keep our eye on it. We certainly wouldn't say that it's because of less miles driven due to gas prices.

Adrian Hennah - *Smith & Nephew - CFO*

And, yes, the Hips and Knees absolute numbers, of course, we don't disclose the specifics so you have to guess that from your previous numbers I guess. Back to you.

Michael Jungling - *Merrill Lynch - Analyst*

Okay, thank you.

David Illingworth - *Smith & Nephew - Chief Executive*

Thanks, Michael. Okay, [Edan].

Unidentified Audience Member

Thank you. I have three questions and a follow-up.

David Illingworth - *Smith & Nephew - Chief Executive*

Of course.

Unidentified Audience Member

The first question is for -- in terms of your Endoscopy margins, you've indicated that that's somewhat being held back by litigation and business development costs which I would expect to be one-offs. Can you give us the underlying Endoscopy margin? That would be great.

The second question is CMS has obviously put their notice out there trying to get comments on the potentials of a NCD for hip Resurfacing. Can you comment on your intentions there? That would be helpful.

The third question is --- I've lost track of it now. Right, the fifth -- the 500 accounts that you're billing for Negative Pressure Wound Therapy, can you give us a sense of the sort of pricing you're getting from those accounts? Obviously, initially, I suppose there was going to be a fair amount of trialing going on. Can you comment on the -- are you actually getting decent sales from those accounts?

And the follow up is really after Michael's question, of your Hip, Knee, Fixation sales growth, excluding Plus. That would be great. The negative impacts of Plus. Thank you.

David Illingworth - *Smith & Nephew - Chief Executive*

All right, well, let's split this up. We don't have a comment on your CMS question because we don't really fully have a position on it or understand as of yet.

On the Endoscopy margins, there's not a lot of detail we can give you, except for the fact that I thought we did actually give you the underlying (multiple speakers).

Adrian Hennah - *Smith & Nephew - CFO*

Well, the easiest way to do it is the combined absolute level in the quarter of those legal fees and business development costs was $4m.

David Illingworth - *Smith & Nephew - Chief Executive*

Yes.

Adrian Hennah - *Smith & Nephew - CFO*

So you just back that out --

David Illingworth - *Smith & Nephew - Chief Executive*

Right.

Adrian Hennah - *Smith & Nephew - CFO*

-- here for Endoscopy.

David Illingworth - *Smith & Nephew - Chief Executive*

Right. And I think the margin, if you correct for that, would have been about 200 basis points as well. Was I right?

Adrian Hennah - *Smith & Nephew - CFO*

(Multiple speakers) [what the number is].

David Illingworth - *Smith & Nephew - Chief Executive*

Yes, I (multiple speakers). From memory, I think it's around 200 basis points of improvement, and those are one-offs. Just to answer your question, yes, they are.

On Negative Pressure Wound Therapy, well we can't give you -- I can't -- obviously, I'm not going to tell you what's going on in pricing, but I will give you some comments about our intent here. Our intent is not to be the low price provider of Negative Pressure Wound Therapy products. Our ultimate goal is to lead this market segment with the best products, the best service and the best range of products. That's our intent.

Now that might take us five years to get there, might take us three years to get there, might take us seven years to get there, it might. I don't know how long it's going to take to get there, but that's our intent. And that's how we're investing in this business and that's how we are trying build our -- this business right now.

So, for us, it's not about -- it's not about going out and bringing a lower price to the marketplace to try to get penetration. We -- we're getting good pricing, we're happy with it, we're not seeing any pressures to do anything other than what we've decided to do on pricing, so I think that's the indication that I would give you.

In terms of the Knee, I kind of lost that while I was writing down the answer.

Adrian Hennah - *Smith & Nephew - CFO*

I think Edan wants us to split the Plus adjustment between Hips and Knees. We're not going to go down to that level, but it's not hugely different between the two. And we've given you the numbers in Recon, so you're not going to be miles adrift if you make the same adjustment for Hips and Knees in percentage terms.

David Illingworth - *Smith & Nephew - Chief Executive*

All right, thank you. Yes. Tom.

Tom Jones - *JP Morgan - Analyst*

Hi. It's Tom Jones from JP Morgan. I've got just two questions, but I do confess, one has two parts. Just on the cost pressures, to follow up on Adrian's comments, I just wonder if you could give us some more detail on particularly where you're seeing cost pressures in your business and how you're thinking about managing those going forward?

And in that same vein, I wondered if you might be able to share some thoughts or guidance on potential Plus cost synergies. I know you gave some guidance initially when you bought Plus, but that guidance has since disappeared from your presentation. So I wondered if you might be able, now things have bedded down a bit, give us some kind of adjusted feel for what kind of cost synergies you think you can achieve?

And then, just to follow up on Dave's question -- statements regarding the fact that you don't expect Hip Resurfacing to be any different in the US to how it is internationally. From that, can we assume that you expect it to, ultimately, pan out at around about 10% of the primary Hip market, or maybe just a little bit shy? And do you expect to have around about a 50% share once you have a full suite of competitors?

David Illingworth - *Smith & Nephew - Chief Executive*

You want me to take a shot at the first, and then you can --? I feel -- it was great; it was a question addressed towards you that I actually think I might be able to answer.

Adrian Hennah - *Smith & Nephew - CFO*

Please, be my guest.

David Illingworth - *Smith & Nephew - Chief Executive*

The -- I don't think we have any different opinion at this point on the -- I'll take the last one first, and then if I need help you can jump in, Adrian.

I don't really think we have any different opinion on how big the Resurfacing market is going to be in the US than we originally speculated on. We have 3.5% of the total volume right now. We're very, very happy with that -- that position after just two years in the marketplace. And it's not the easiest thing in the world driving adoption of a technology when you're, for a long period of time, the only competitor in the marketplace, and one that has about 10% market share in that segment to begin with in terms of Hips in the US.

So we're very pleased with where we are. I wouldn't change that prediction. We've seen outside the US in developed markets that it's somewhere in that range, 8% to 10%. And I guess we'll see what the adoption curve is going to bring.

In terms of cost synergies, we haven't changed our guidance or our confidence in our ability to bring cost synergies from the Plus acquisition. And I don't know the exact number that we detailed out, was $40m? Yes, it was $40m, and we haven't changed that at all. In fact, I think we're ahead of plan from what I understand from the last time I've looked at the numbers. I think we might be slightly ahead of where we thought we might be at this point in time, given some of the issues we've been dealing with.

Adrian Hennah - *Smith & Nephew - CFO*

(inaudible) and one thing for that, I think Tom is probably saying, yes, that's all very well but you've lost a third of the sales. And there's two elements to it therefore, Tom, that's quite right. We are absolutely on track, at least on track with the $40m by the third full year, which we said we would. In addition, as we've said, we're going to contain the margin on the lost $100m to 25 basis points. That implies we're taking out costs over and above that $40m, which we're clearly going to do.

In simple terms, as you know, we started off at the earnings improvement phase with a 20.5% margin and said an average of a percent a year. We said dilution from Plus, but it will get back up to the same level with integration synergies. Well, that is still our view. It's still our view that when you get through that, notwithstanding this lost $100m, those four percentage points will be there at the end of the fourth full year, albeit with this dilution in the middle.

David Illingworth - *Smith & Nephew - Chief Executive*

In terms of the cost pressures that we have, I think you can pretty much figure out where they are; they are in some of the metals area. But we have a very low percentage of material costs that goes into the pricing of our products. We have healthy gross margins and we've been able to deal with that along the way. We have a lot of productivity programs in place. We talked about the ID program. There's a lot of things going on in manufacturing and procurement etc., that would we be happier if we didn't have to deal with some of these material cost increases. Yes, we would, because then we could claim more victories somewhere else. But the fact of the matter is we're dealing with it along the way. Now, if it gets to the point where we feel like it might be a little bit more difficult to deal with it, we'll signal it in some way. But, at this point in time, we've been able to manage it.

Yes, Martin. One more from here. Sorry to the operator; we'll take one more from here.

Unidentified Audience Member

Thanks, I'll limit myself to two. First question comes back to some of the stuff you've talked about in the past, about how you're selling Arthroscopy and Hip and Knee products to the same surgeons, and how you're going to try and lever that. Obviously, there's been very little mention of that in this presentation and, of course, we note you're putting Trauma back in with orthopedics, but nothing in relation to arthroscopy, Endoscopy. Could you give us some idea of what your intentions are in this area from here? Have you given up on that, or do you still think there's something to be gained by that level of cross-selling?

David Illingworth - *Smith & Nephew - Chief Executive*

Well, I think there's something to be gained but I don't want to create some hysteria over something that we haven't planned to do. I believe that if you look out into the future that you're going to see more emphasis placed around a disease state versus an artificial segmentation by the way we manage our business. I think we have to respond to our customers.

And when an orthopedic surgeon -- if you think about an orthopedic surgeon, and I've said this before, you go in and you present yourself with some knee pain, they don't immediately say, "great, knee pain; I'm going to schedule you for a knee replacement". They do their radiographs and then they do MRIs and they try to give you an injection and they inject you with some steroids and cortisone and then they give you some Supartz, and before you know it they're going in there and cleaning it up with arthroscopy and then later on --

So they're dealing with this disease state as it progresses and I think that there is some value in making sure that we're collaborative as a Company around those customers and those disease states. We shouldn't make it artificially hard for them to deal with us. They shouldn't have to dial one number, 1-800-endoscopy one day and 1-800-ortho the next. We've just got to make it very easy. It doesn't mean we're going to take away those customer front ends but we have to make it easy.

It's interesting to hear the questions about, okay, you separated Trauma and Recon and then you put them back together. You know what, they're still in the same building they were always in. Their offices are next to each other. It's not like -- the folks in Memphis don't see it that way. They still pull into the same parking lot and the same operator answers the phone. We just took away the barrier that we created for ourselves by having different sales management teams at the customer face. And we'll continue to do that.

I am a customer nut when it comes to trying to figure out how to run this business. I want to make sure our customers are serviced properly. And that's the whole tone around us; it's not like you should be expecting any grand announcement any time soon.

Unidentified Audience Member

Okay. And a quick one for Adrian. Maybe you'd just like to comment on how we should think about phasing across Q3 and Q4 of your full-year guidance. And I think the assumption would be that Q4's going to be much stronger than Q3, but I don't know if you'd like to add at all to that.

Adrian Hennah - *Smith & Nephew - CFO*

Martin, nothing to add. There's nothing to draw attention to other than the normal seasonality you'd expect between Q3 and Q4. We don't want to draw anything specific in for quarter three or quarter four.

David Illingworth - *Smith & Nephew - Chief Executive*

Thank you, Martin. We'll go to the operator.

Operator

Thank you. We'll take our next question from Hans Bostrom of Goldman Sachs. Please go ahead.

Hans Bostrom - *Goldman Sachs International Ltd. - Analyst*

Good afternoon, gentlemen. I have three questions as well. First, if you could confirm that the impact from Plus in terms of lost revenues will be as much as $65m for the second half of the year. Is that how we should see that in view of what you have said of $100m annualized?

Secondly, you talked in Q1 about an increase in your R&D costs towards, I believe, the 5% of revenue target, but you're still well short of that. So, just so we get a sense of how that is going to develop for the full year in terms of percent of revenues and, indeed, if it's going to take well into 2009 before we get close to the 5% target?

And, thirdly, I would like to understand if the figure that I calculate myself on terms of NPWT sales just being $3m or $4m in the US in the quarter, is that correct, in view of the growth that you gave with or without NPWT in the US?

And also if you could maybe discuss a bit around the statement you made that the continued launch costs of NPWT will continue to depress the margins. That sounds somewhat more conservative than the previous guidance, I believe, was that the margins would be back on track second half of the year. Thank you very much.

David Illingworth - *Smith & Nephew - Chief Executive*

Right, we'll split this up, kind of double team this a little bit, Adrian. Well, the answer to the first one is, no. You want to give a little more color behind that?

Adrian Hennah - *Smith & Nephew - CFO*

Yes, it's no. You may have done the calculations, so it's $35m to date. $100m minus $35m is $65m. Well, you're right until the last bit of that calculation, in that you shouldn't be using $100m. We haven't said it's going to be $100m in 2008. We've said there'll be $100m in a full year, in a full 12-month effect, once it's washed its way through the system, and somewhat less than that in 2008. So, no, we do not expect it to be $65m in the second half. That's the correct answer, Dave.

David Illingworth - *Smith & Nephew - Chief Executive*

On the R&D costs, we are dealing with some of the -- not some. We're dealing with the same issues that everybody's dealing with in terms of trying to spend our money as quickly as we'd like to in that area. We have been slowed down somewhat due to the monitoring of our spend in this area, and that's just a fact.

Do we think we'll get some catch up at some point? Yes, but we don't know exactly when. We haven't really sat down to think about what the phasing is. But I think you'd see it returned, if not by the end of the year, probably by the beginning of next year, that level that we talked about. We're still working our way through the learning curve here, in the new way of doing things in this area. And that's really the only thing that's driving that in a big way.

Adrian Hennah - *Smith & Nephew - CFO*

(inaudible) and I guess, Hans, there are actually two phenomena here. One is we always said the 5% was in the same time frame as the EIP, so in terms of getting the 5% fairly stable across that sort of timeframe. There's clearly, as Dave points out, a short-term effect that all the Recon companies are facing as a result of the monitor's activities in the US. So we've gone off trend, if you like. You would expect it to be going up slowly. Well, it's gone down, but that's a temporary effect.

David Illingworth - *Smith & Nephew - Chief Executive*

And as far as Negative Pressure in the US, we're not giving actual numbers on that. If you're smart enough to figure out directionally where we are in certain areas, it's a guess on your part, I think.

Adrian Hennah - *Smith & Nephew - CFO*

Obviously, we said -- when we said that the non-NPWT was basically flat, it's not a difficult calculation for Hans to do and, so, well done, Hans.

Hans Bostrom - *Goldman Sachs International Ltd. - Analyst*

So, could you comment a bit, both, given your very positive statements about having recruited 500 customers, when will these customers start to order? And how should we think about that, because you clearly give very positive signals about the Wound Care business for the second half. Admittedly, internationally perhaps most, but also I think you mentioned the Negative Pressure Wound Therapy business in the US. If you could give us a sense of how that will pan out for the second half of the year, and also specifically answer the question on the margin guidance for AWM?

David Illingworth - *Smith & Nephew - Chief Executive*

Right, I'll take the first part and hand the second part over to you, Adrian.

I think it's prudent to continue to exercise some caution here in how excited you get about this. Yes, we have 500 accounts, but you have to understand the dynamics of what's happening here. We have evaluations going on; they're evaluating whether or not our product is a viable product for them to use in their account. They go through a long detailed, whatever they're doing for their individual valuation, they get to the endpoint and they say, yes, this product works. Yes, the KCI product works.

And what typically happens is -- it's not like they say okay, well, since Smith & Nephew's product works we're going to throw these guys out on the street. I think what's happening in reality is that they begin to use our product. It takes time to build up the credibility. They want to see not only does the product work they want to see whether or not we have the Company behind it to provide the service, because there's a service model that's been established by our competition that's firmly entrenched and they do a good job. And they want us to prove that we're doing the right thing.

So we get -- they bring some units in and they have a certain number of pumps in their hospital, or whatever care setting they're in, they start using it, they see that we're doing a good job for them, and our hope over time is that we can build up that credibility and continue to make progress.

So, it is -- I've described it this way before and it is absolutely accurate. It is a little bit like a snowball going down a hill -- mountain, where it just builds up and picks up steam along the way. Because of the fact that it's a rental type model that's been predominantly dictated by the competition, you build up a head of steam, a very little head of steam early, with smaller payments versus the acquisition of the capital equipment, and then you start building up that revenue over time. We're very happy with where we are. We're very committed to this marketplace. We have a good product; it works. We're putting the investment in it and because of that you're going to continue to see this to be somewhat of a drag on the Wound Care business in the US, because it is worth the investment. This is what we want to do.

Adrian Hennah - *Smith & Nephew - CFO*

I haven't got anything to add to that, Dave, other than observing the metaphor of a snowball picking up steam is an interesting one.

David Illingworth - *Smith & Nephew - Chief Executive*

Yes, I guess -- I do have a tendency to mix my metaphors, don't I. Sorry.

Hans Bostrom - *Goldman Sachs International Ltd. - Analyst*

(inaudible) finalize this. My understanding was your guidance before was that the margin in AWM would be on par with '07 in the second half of the year. Is that still the case?

Adrian Hennah - *Smith & Nephew - CFO*

Sorry, Hans, could you say that again?

Hans Bostrom - *Goldman Sachs International Ltd. - Analyst*

My understanding from your previous guidance was the margin in AWM would be on par with the previous year in the second half of the year. Is that still the case in view of what you just said about --?

Adrian Hennah - *Smith & Nephew - CFO*

We don't give guidance at the level of specific businesses, Hans. We're not getting into that trap because we need to invest, we need to have the flexibility to do that. We're not intending -- in the phrase that you're picking up from what I said, we're not intending to change guidance. We're just trying to point out that all along that there are uncertainties we develop this product, uncertainties in the exact levels of investment. We're talking about fairly small numbers here.

So, if you want to push the development of a variant of NPW ahead of it faster, we don't want to stop doing that because we're going to change the margins in the quarter. So we're not intending to signal any change here, Hans. That's all.

David Illingworth - *Smith & Nephew - Chief Executive*

Thanks, Hans.

David Adlington - *JP Morgan Cazenove Ltd. - Analyst*

Hi, David Adlington at Cazenove. Just one question on Wound Management. You've got good European growth this quarter, that's in contrast to Coloplast last week. I assume you're taking share from them. I'm just wondering what's driving that. Is it the new product launches or pricing, or what?

David Illingworth - *Smith & Nephew - Chief Executive*

I think we still need to analyze that, David, I guess is the honest answer. I would hope that we're taking share from them. I saw their results and I think we're still trying to digest them a little bit. We're happy with the progress we're making. We're seeing good -- well, not good, we're seeing excellent results from our European business.

It is the -- I think it's one of the strongest performances in our European Wound Care businesses that we've had in a long time. So, I think the team -- I can tell you the team is very excited about it. They're very bullish on the prospects and I would certainly hope that we're taking share, but I can't give you a lot of good detail around that at this point.

David Adlington - *JP Morgan Cazenove Ltd. - Analyst*

Thanks. And then just looking forward to next year in Wound Management, you've clearly got some sales that have been hit in the US this year. How should we be thinking about growth relative to market for next year for Wound Management?

David Illingworth - *Smith & Nephew - Chief Executive*

Well, we don't really know what the growth in the market's going to be. It's an interesting dynamic for us. We saw some of the results of our competition came out that I'm sure you saw as well, and it was a little bit weaker, and actually brought down some of the global growth rates in Wound Care.

It was one of the reasons why we woke up one day and said, wow, we grew faster than the global market in Wound Care. And we reported on that. We feel pretty darn good about it. But we really didn't think we were going to be at that point until we saw some of the results from what was going on with some of the competition, specifically, the other Negative Pressure company.

So we're still trying to figure out exactly what the growth rates are going to be. We think -- it's an interesting dynamic, David, because we have this very well developed market in the US with Negative Pressure that, essentially, we start from zero on. The market's already developed.

Any share that we take is going to be almost like incrementals, well, it's incremental share for us and it's just this incremental growth. So it's a very different dynamic for us than other competitors in the marketplace because we're going after this sacred segment that was really only out there being serviced by one company. So it's a bit of an odd dynamic.

Any more? Okay, one additional follow up.

Tom Jones - *JP Morgan - Analyst*

I just wondered if you wanted to make some comment on how you see the Negative Pressure Wound Therapy market panning out in the post 2014 and beyond timeframe when EIP comes back into question. Because it seems that KCI is trying to diverse out of negative pressure wound therapy as fast as you're trying to diversity into it. And so I just wondered what your very long-term view on that is.

And the second question is, just one for Adrian. I notice that you -- in the final markups of Plus you've reclassified a fair bunch of the goodwill intangible assets. Does that affect the amortization going forward, or the tax position on those -- the amortization of those intangibles?

David Illingworth - *Smith & Nephew - Chief Executive*

I'll take the first part of it. I don't see anything unusual about a single-product company trying to diversify. So, for what it's worth, I don't see anything odd with that. I would expect them to diversify. It would make total sense strategically if I was running that business. So that doesn't surprise me at all. I think the difference is that we are already diversified.

We've hundreds of products that we're taking into these accounts today. We treat more hard-to-heal wounds than any company in the world. And we have a full range of products, full range of dressings, tissue healing products and we are actually adding to our portfolio. So I think it's entirely consistent. I wouldn't draw any strange dynamic there. In terms of the second half of the question, Adrian, it's all yours.

Adrian Hennah - *Smith & Nephew - CFO*

Nothing very strange going here, Tom. You've got one year, as you know, under IAS 36 to true up the allocation of the consideration between goodwill and acquisition intangibles. Well, this was the year anniversary, so we did that. There was a minor adjustment -- or was an adjustment and that did impact the amortization charge in the period. And, therefore, we did draw attention to the fact that, on an ongoing basis, we expect amortization of acquisition intangibles to be about $10m a quarter as compared to the slightly lower number in this particular quarter.

Tom Jones - *JP Morgan - Analyst*

Sorry, just to quickly follow up on that. I assume you tested Plus for an impairment, given that you have to under IFRS, but IFRS very kindly gives you an out in that you can offset that Plus, that write down, against internally-generated goodwill. Just out of interest, when you did the impairment, what was the number?

Adrian Hennah - *Smith & Nephew - CFO*

Well, you're right. You're right on many counts here, Tom. First of all, I think we could certainly acknowledge that the value of Plus is less than it was when we bought that. As to how much less, I think that's a matter for the judicial process, the arbitration process, that is underway.

You're quite right that under IAS 36 we do not need to -- or, at least, we have to look at the relevant cash generating unit, which is the whole of Recon. So, clearly, no impairment is required. And that's not our choice; that's what the rules say and the fact that our predetermined policy was that Recon was the cash-generating unit. So, no, we're not going to give you that number.

David Illingworth - *Smith & Nephew - Chief Executive*

Okay, on the Internet we saw a couple of questions. Okay. There are still plenty.

We'll take a couple, in the interests of time, so, go ahead.

Operator

Thank you. We'll take our next question from Joanne Wuensch of BMO Capital Markets. Please go ahead.

Unidentified Speaker

Hi, this is Nat for Joanne. Thanks for taking her question. I was wondering if you could go into your Hip business for a second and speak to whether or not you see an impact from the recall and now the voluntary suspension of Durom Hips in the US.

And then also on Hip Resurfacing, you've spoke a little bit about it. You had a tough comp, you've seen some competitive pressure, but you've also said that it's been a tough row to hoe being the only competitor in the market in the US. So if you could speak a little bit to how you see another competitor coming in as being a help and a hindrance in the near and long term, that would be very helpful.

David Illingworth - *Smith & Nephew - Chief Executive*

Okay. Well, on the first piece, I'm not sure we're the best Company to ask about getting benefits from the recall of the -- I assume you're referring to the [Durom] recall on Hips. Because we don't have a large metal-on-metal Hip that's approved for primary application in the US, so I don't think we would be the primary beneficiary of that. So, we may be seeing a little bit here and there, but I don't think it's substantial.

My comment on the -- I don't think I used the words a tough row to hoe, but it wouldn't be real far away from the truth. Markets are easier to develop when you have competition, especially when you have companies that have 90% of the market share telling their customers that they shouldn't buy it, that there might be something wrong with it. And it's just a fact when you have multiple competitors in a marketplace, the marketplace gets developed faster. The adoption curves are quicker. I think that's a marketing and economic fact based on history.

I think given that, the fact that we have 3.5% penetration, we have 3.5% of the volume of the Hip market in the US, when we are substantially the only competitor in this marketplace is pretty darn good. I think it's pretty darn good, and I'm happy with it. And that was what I meant by it, but does it -- to specifically answer your question, does it help us to have more competitors in the marketplace? I think it does in this case. Because I think the market gets developed faster and we've already proven that we can compete.

Outside the US, we've been competing with a very healthy set of competitors for years now, and we have over 50% of that market share on a global basis. So we're quite confident in our ability to compete and I think if the adoption rate gets increased, if the slope of that adoption curve gets steeper, then I think we're going to benefit from it.

Unidentified Speaker

Thank you. Just a follow up. Although you don't have the metal on metal, do you think that the Durom recall has had any negative impact on the market overall in terms of the questions that doctors are having, or patients are having now, given the high profile troubles?

David Illingworth - *Smith & Nephew - Chief Executive*

I'd have to guess at the answer, but I'll give you my guess. My guess is probably not. Not an overarching impact on the market in general. I don't think there's a loss of confidence in some of these products, or Hips in general, or the metal on metal, as a result of it. We do have a metal-on-metal bearing surface in the VHR and it works great. So, I think I'd probably answer that question with a no, but I don't have a lot of real facts to back that up. It's an opinion.

Unidentified Speaker

Okay, thank you very much.

David Illingworth - *Smith & Nephew - Chief Executive*

Another one online, so we can clear out the large line of --

Operator

Thank you. We'll take our next question from Ilan Chaitowitz of Redburn Partners. Please go ahead.

Ilan Chaitowitz - *Redburn Partners LLP - Analyst*

Good afternoon, this is Ilan Chaitowitz from Redburn in London. Three questions, the first two related. Firstly, it was my understanding with Plus that there was one particular geographic region that was responsible for just under two thirds of the $100m. Now, I was wondering if there's been any deterioration in that geography or spill over into any other geographies since we last heard from you at the Q1 that you could comment on.

And secondly, related to that question, we've seen a run rate of about $35m for the first half this year, and I know we've talked about this a lot on the call, but why do you expect that run rate to deteriorate over the next six to 12 months?

And the final question relates to a spiking cost that we've seen from some of your competitors relating to compliance programs. Do you see any risk over the next 12 months, say, of Smith & Nephew having to ramp up its costs relating to any compliance or monitoring programs?

David Illingworth - *Smith & Nephew - Chief Executive*

Let me take the first one. I didn't quite get the second question; I'm conferring with Adrian. The simple answer to the first question is, no, there is no spill over from the Greece situation that we had and there's no further deterioration because it deteriorated very quickly. And what happened, happened. And we essentially have shut down our business there to the point where we have severed our relationships and are establishing a direct operation there. So we're starting from a very small base of very close to zero. So the real simply answer to that is, no and no.

Adrian Hennah - *Smith & Nephew - CFO*

To your second question, Ilan, I think it might be helpful just to understand a little more about how we got to the $100m. And we said with the quarter one results that we felt we had good line of sight on all the unacceptable practices and had stopped them. And that, in the case of those in Greece, there had been a very quick impact between stopping the practices and sales disappearing. But in other geographies we were not expecting there -- it was very quick and very complete, as they say.

In other geographies, we were not expecting it to be as complete or as quick. So, for us, the issue is not so much are there any other nasty practices out there, and subsequent months confirmed we did have good line of sight to all of them, but what will the reaction be to us stopping those unacceptable business practices. That's where the judgment lies and that's why the $100m was a judgment.

What you're seeing is, the increase went from $16m in the first quarter to $19m in the second quarter, is some effect coming through. We still don't know exactly what that will be, so it is still a judgment, $100m, but a $100m still remains our best judgment. And we'll see whether that's exactly right or not but it's our best judgment and it hasn't changed for the last quarter.

David Illingworth - *Smith & Nephew - Chief Executive*

Okay, well, we do have an issue with time, so we're going to have to end it here.

Adrian Hennah - *Smith & Nephew - CFO*

So, maybe just do the third (multiple speakers).

David Illingworth - *Smith & Nephew - Chief Executive*

There was another one; I'm sorry.

Adrian Hennah - *Smith & Nephew - CFO*

On the cost of compliance, yes, we're no different from the other US players or global players with US orientation. That said, the cost of compliance is going up for us too. The cost of the monitor in the short term and the cost of compliance, that doesn't affect our margin guidance, but it's certainly one of the pressures. Frankly, more so than the cost of metals by some significant way that we're dealing with. Thank you.

David Illingworth - *Smith & Nephew - Chief Executive*

Right. Well, thank you very much. I appreciate everybody attending and the thoughtful questions, and we'll see you next time.

Adrian Hennah - *Smith & Nephew - CFO*

Thank you.