Smith+Nephew

Third Quarter 2020 Trading Update

Thursday, 29th October 2020

Operator: Ladies and gentlemen, thank you for standing by and welcome to the Smith & Nephew PLC Third Quarter Results Presentation. At this time, all participants are in a listen-only mode. After the speaker presentation, there will be the question-and-answer session. To ask a question during the session, you need to press star and one on your telephone keypad. I must advise you that this conference is being recorded today on 29th October 2020.

Safe harbour

Certain statements in this presentation are forward-looking statements. These statements are based on Management's current expectations and are subject to uncertainty and changes in circumstances. Actual results may differ materially from those included in these statements due to a variety of factors. More information about these factors is contained in the Company's filing with the Securities and Exchange Commission.

I would now like to hand the conference over to Roland Diggelmann. Please go ahead, sir.

Overview

Roland Diggelmann

CEO, Smith & Nephew Plc

Q3 trading update

Significant improvement in Q3 trading over Q2

Thank you, Nadia. Good morning, everyone, and welcome to Smith & Nephew's Third Quarter 2020 Trading Update. I'm also joined today by Anne-Françoise Nesmes, who I'm very delighted to have with us for her first results call as a Chief Financial Officer.

Let me just start with a few high-level remarks. Firstly, I'm very pleased with our progress in the third quarter and especially how the business and our employees have responded to the challenging circumstances. We've see most of our global markets recover. Thanks to our work in Q2, we were actually ready.

Continued strategic progress to transform the Group

Our commitment to maintaining strong customer relationships, keeping our supply chain and manufacturing open, and investing in both retaining and training our people is paying off. Anne-Françoise will take you through our Q3 performance by markets and trading conditions, and then I'll cover the performance of the franchises.

Stepping back from the quarter to look across the year, I'm also very pleased that we have continued to deliver on our strategy, while also responding to COVID-19 effectively. We have made great progress before COVID. We had great momentum in the second half of 2019 and we've continued to – the important work to transform the Group.

Responding effectively and emerging a stronger organisation

I'm proud of the way the team has delivered on multiple fronts. Those include major product launches, M&A, R&D, and pushing forward our people and sustainability agendas. I will develop some of these themes with examples of what we've been doing to further enhance our mid-term growth profile in the presentation later.

But first, let me hand over to Anne-Françoise to lead off the review of the quarter.

Q3 2020 Financial Review

Anne-Françoise Nesmes

CFO, Smith & Nephew Plc

Q3 revenue

$1.2 billion, -4.2% underlying, -3.7% reported

Thank you, Roland. Good morning, everyone. As Roland said, it's my first results call with you and I'd like to say that I'm delighted to be here at Smith & Nephew and I also look forward to meeting you in person whenever it will be possible to do so again.

Now, moving to the numbers. Q3 revenue at $1.2 billion declined by 4.2% on an underlying basis and 3.7% on a reported basis, in line with the announcement we made on 1st October. Pleasingly, the US, our largest market, returned to growth in the quarter at 0.9% on an underlying basis, with revenue of $630 million. Of course, given the different recovery profiles, Other Established Markets declined by 6.2% and Emerging Markets by 14.5%.

Quarterly underlying sales development by region

US

Now, looking into the detail of each region for Q3, we saw a general continuation of the patterns that had developed in Q2. As I mentioned before, and you can see on this slide, the US business continued to improve and returned to growth for the quarter. And as a reminder, by the end of Q2, surgery had restarted in all states, but with restrictions in some. By the end of Q3, the restrictions in Texas had been relaxed and lifted entirely everywhere else.

Established Markets

The picture in our Established Markets is very mixed. Markets that were fastest to recover initially have continued to lead the way. In Europe, for instance, Germany and France returned to growth in the quarter, and Southern Europe also improved. However, as we saw in Q2, the UK continued to be slower to recover with surgical volumes still significantly below the prior year.

For Established Markets in Asia Pacific, Australia procedure volumes recovered further to approximately 90% of normal level by early October, and Japan is now at similar level after lifting restrictions in the quarter.

It is important to note, though, that there is still uncertainty in our Established Markets. We have seen some postponements and cancellations of procedures recently and it's not yet clear what the impact will be as new restrictions are being reintroduced. Additionally, the levels of growth in some European countries may reflect the systems working through the backlog of deferred treatments.

Emerging Markets

Finally, looking at our Emerging Markets, they showed divergent performance. What looks like a relatively unchanged rate of decline over the quarters is, in fact, driven by markets entering and exiting restrictions at different times.

Q1 weakness was driven by China, as we know the first market to have COVID restrictions. But China recovered strongly in Q2 and again grew in Q3, as a whole. Capacity utilisation remains over 80%.

Q2 and Q3 weaknesses was instead driven by other Emerging Markets that were impacted by COVID later. These markets were still largely under restrictions as we exited Q3. For instance, India, South Africa, and many Latin American markets have yet to show sign of recovery.

Q3 recover, visibility still limited

COVID-19 significant uncertainty continues

Clearly, we are all interested in how the rest of 2020 and 2021 may develop. Unfortunately, visibility remains limited. As I've just explained, very significant geographical variability, including local restrictions being reintroduced in some markets.

In general, we do believe healthcare systems are better prepared than they were earlier in the year and we do not expect the same global impact as we saw in Q2. However, we still expect some impact. While it's too early to quantify, we've seen increasing postponements of surgeries in the last few weeks in a number of European countries.

Full-year 2020 guidance remains withdrawn

As a result, our full-year 2020 guidance remains withdrawn since the nature and the scope of any new restrictions to control COVID-19 through the year-end are not known. On listening to public health authorities and observing developments at the late – this latest stage of 2020, you will not be surprised to hear that our expectation is that the impact of COVID will continue in the first half of 2021.

Focussed on delivering growth, investments sustained

But having said all this, it's important to remember that our strategic focus remains on delivering long-term growth and we are investing accordingly. We are continuing to prioritise R&D investment. We have continued with our M&A agenda, which brings additional short-term margin dilution.

Negative operating leverage while volumes reduced

And naturally, you should also expect the negative operating leverage effects we described earlier in the year to continue whilst volumes are under pressure. As we said before, we have been preparing new operational efficiency plans, which I have been reviewing since I joined. A significant component of the plan is around manufacturing. But as you know, manufacturing and supply chain transformation takes time to execute.

Transactional FX headwind

And finally, as you look into 2020 and 2021, I would like to remind you that the revenue headwinds from foreign exchange should result in a transactional headwind for the trading margin in both years.

And with that, I'll hand back to Roland to cover our franchise performance and our strategic progress.

Franchise Performance and Strategic Progress

Roland Diggelmann

CEO, Smith & Nephew Plc

Q3 revenue

$1.2 billion, -4.2% underlying, -3.7% reported

Thank you, Anne-Françoise. Moving on to the franchises, indeed. All three showed significant improvement, both over Q2 and over the June growth rates. Orthopaedics declined by 2.8% globally, Sports Med and ENT by -4.5%, and AWM by -6.1%. Regional patterns within the franchises were largely similar to those of the Group.

Orthopaedics: $512 million, -2.8% underlying

Hips

Moving to Orthopaedics, we continue to see a stronger performance in hips than in knees. As well as a higher proportion of emergency cases in the hip market, surgeons also appeared to be preferentially treating hips. For us at Smith & Nephew, specifically, we're seeing additional strong growth from the rollout of our OR3O Dual Mobility Hip System.

Knees

In July, we announced the US launch of CORI, our new generation robotic surgery platform for total and UNI knee arthroplasty. Customer reaction from the new form factor has been overwhelmingly positive as it meets the needs for a smaller, more portable robotic system.

Other Reconstruction

Other Reconstruction declined 3.1% in the quarter, including a return to growth in the US. That reflected recovery in capital sales, along with the week prior-year quarter for the acquired Brainlab orthopaedic recon business.

Trauma

Trauma continues to improve, with growth in the US and Asia-Pacific for the quarter, as well as for plates and screws and our hip fracture business, globally.

Sports Medicine and ENT: $350 million, -4.5% underlying

Sports Medicine Joint Repair

In Sports Medicine, Joint Repair declined 2.7%. This was really driven by recovering elective surgery volumes, although lower than normal levels of competitive sports activity remained a drag on some specific knee procedures.

Arthroscopic Enabling Technologies

In markets where procedure volumes are recovering, AET capital sales have also recovered. Our pipeline of business remains good and we're seeing a step-up in evaluations, particularly around the LENS 4K Imaging System.

ENT

ENT has been slower to recover. Understandable caution from parents, in particular, has remained the drag on growth. However, we did start to see some improvements late in the quarter in the US. Our focus in ENT has been on readiness for the recovery with the rollout of HALO COBLATION Wands and training surgeons to use the Tula tympanostomy system. Revenue for Tula has been slow so far with lower ear infection rates, as a result of COVID restrictions. We've effectively lost 12 months, but we're continuing to invest, for example, in additional clinical studies and, of course, on market readiness.

Advanced Wound Management: $338 million, -6.1% underlying

In Advanced Wound Management, all three segments showed improvements over Q2 although, as expected, recovery has been slower than in the surgical business. The factors include a higher proportion of sales coming from Europe, specific to us, restricted access to OR cases for non-essential staff in many regions, and key acute hospitals staff remaining focussed on COVID care.

Advanced Wound Care, Advanced Wound Bioactives, and Advanced Wound Devices

In AWC, we saw significant improvement in the US and in Europe, including some European markets returning to growth. Bioactive sales declined 4.5%. Debridement and skin substitute market volumes were down by single-digit percentage, with improvement in the – later in the quarter. Advanced Wound Devices declined 6.9%, with the overall recovery mainly driven by the US.

Sustaining investment

Integra Orthopaedic Extremities acquisition – expanding in high-growth segment

Deal benefits of acquiring this comprehensive portfolio of extremities assets

I'd like to finish by spending some time on what we've done to enhance our mid-term growth profile and in line with our strategic imperatives. In September, we announced a conditional agreement to acquire Integra's orthopaedics extremities business.

Extremities is a market we've viewed as attractive for some time. It's a high-growth category with 67% growth in the US extremities market, clearly accretive to our current weighted average market growth rate. The asset is also synergistic with our existing business. As with many of our tuck-in acquisitions, we have the ability to sell the acquired portfolio through significantly wider-reaching channels than it's been sold through today.

Our retail and sports sellers are already calling on surgeons that also perform shoulder arthroplasty. We will now be able to sell them as Smith & Nephew shoulders. For our Trauma business, we are already calling foot and ankle surgeons and upper extremities, and Integra products will further enhance our offering there. And the asset brings a team of

Extremities specialists into Smith & Nephew with established distribution capabilities of their own that we can also benefit from.

Finally, the transaction adds to our pipeline with a next-generation shoulder, bringing short-stem and stemless technology into the portfolio, and expected to launch in 2022. With these opportunities, we expect to drive double-digit revenue growth for the acquired products.

Meaningful new revenue growth drivers accumulating across the portfolio

New launches from R&D

You should see the Integra transaction in the context of the broader strategic progress we've made this year. We've been building on the progress of 2019 and established further drivers of growth. Firstly, you've seen important product launches from our internal R&D. We covered the technical differentiation of CORI and INTELLIO at our analyst event in September.

We've talked less about HALO, but it's an important launch in ENT. HALO brings our last generation of COBLATION technology to tonsil and adenoid surgery, ready for recovery in that part of the market. All three of these launches can also drive both capital and consumables. And we have a full pipeline still coming. To pick just one example, the next generation of PICO, which we expect to launch in late '21, following regulatory clearances and the various approvals.

Adding growth through M&A

Secondly, we've made further progress in adding growth through M&A. The recent Integra transaction and Tusker in January are examples of the tuck-in acquisition strategy that's familiar to you by now. We've also added to our digital technology capability.

The MiJourney acquisition lay the foundation for ARIA, our digital platform to connect providers across the patient's episode of care and that we believe will enable the reduction of post-acute cost, improvement of clinical efficiencies, and the generation of value-based data sets. The technology has potentially broad applications, but is particularly suited to the high-growth ASC segment.

And finally, we will continue to expand the acquired assets from previous years. We have successfully completed requirements for CE marking REGENETEN and NOVOSTITCH PRO, both of which we – were – we acquired as US assets. And then in Wound, we have now fully trained our US bioactive field force to sell Grafix and Stravix and start driving the revenue synergies of the Osiris acquisition.

So between these various steps, we have put additional and meaningful mid-term growth drivers in place across all three franchises.

Summary

In summary, I return to my opening slide. Q3 was significantly better than Q2. And I would like to take this opportunity to also thank all of our employees globally for the way they have responded in these difficult and challenging times, and for remaining focussed on supporting customers and patients through the crisis. COVID-19, as we all know, has not stopped, but we will continue to work on important measures to transform Smith & Nephew, and I'm very excited by our progress here.

Future outlook

And finally, what about the future? Smith & Nephew is now a company with a purpose and a plan. We focus on what we can control. This is commercial excellence, delivering on our R&D pipeline, building our culture, and driving efficiency. The Smith & Nephew of today is more agile and we have proven able to respond rapidly to changing circumstances.

Looking further ahead, we're building a stronger company. We have a proven strategy, excellent Management team, and a robust balance sheet. When we move beyond COVID?19, we will remain committed to our mid-term ambition to consistently outgrow our markets at the same time as delivering improvements to our trading profit margin.

With that, I thank you for your attention. Anne-Françoise and I would now be very happy to take your questions. Thank you.

Q&A

Operator: Thank you. Ladies and gentlemen, we'll now begin the question-and-answer session. If you wish to ask a question, please star and one on your telephone keypad and wait for your name to be announced.

The first question comes from the line of Tom Jones from Berenberg. Please ask your question.

Tom Jones (Berenberg Bank): Good morning. I had a couple of questions. Thank you for taking them.

The first is, I just wondered if you could shed a little bit more colour on the differential between the Hip and Knee growth that you saw in the quarter. Do you think that's broadly reflective of the market or do you think there were some Smith & Nephew specific factors beyond OR3O that are playing into that? And I guess the question is, what do you think the sort of near-term outlook for both the Hip and Knee businesses is? Do you expect that differential to continue?

And the second question I had was really on Integra. Your guidance that you expect to exceed your WACC in Year Five is probably one to two years longer than usual. Does this just reflect the sort of – you know, the fact you're not expecting new shoulder until 2022 or, you know, is it perhaps more symptomatic that the good acquisitions are just getting a little bit harder to find, so you're having to push the boundaries of what's acceptable, in terms of a ROIC WACC spread and the time to achieve that positive spread?

Roland Diggelmann: Thank you, Tom. Thanks for the questions. I'll take the first one on Hip and Knee differentials.

First, I think there is probably going to be a market factor and then a specific factor to Smith & Nephew. So in Hips, what we're seeing? We're seeing more emergency, reconstruction, or also trauma. That's certainly a fact. There is probably surgeons that treat hips further or more earlier than knees, in the broader context. So from that end, we expect that differential to continue.

And then, on the portfolio-specific side, as you pointed out, we've had great success with OR3O. It's still only at the beginning of the launch. So we expect that to continue to deliver strong growth numbers for us.

And then, on the Knee side, we still don't have a – you know, we're working hard on having a porous offering as well. So I think that will also continue to have a certain impact and underpin the differential.

On the Integra acquisition, I think you're absolutely right. We have to differentiate between the type of acquisitions, of course. And if it's more technology-based, in the case of Integra, I would say, it's mixed technology.

As you pointed out, we have a shoulder that's in development, which we're very excited about, which will only come in '22. And it's a commercial play as well because we acquired commercial capabilities. But typically, acquisitions in technology probably take a bit more time to return on – with the return on investment.

Tom Jones: Okay. That's very helpful. And then, maybe one quick follow-up, maybe for Anne-Françoise. Welcome to Smith & Nephew.

I was just – it's – it was on the bond issue really. I mean, Smith & Nephew is a company that has historically relied more on bank debt than bond debt. So I just wondered if we should be reading anything into the fact you've been a little bit more aggressive on the bond side here? And is that just about locking in attractive interest rates for a long period of time or is that about, you know, reducing refinancing risk and pushing the maturity profile out quite some distance?

Anne-Françoise Nesmes: Thank you, Tom, for your question. Nice to meet you virtually, so to speak.

So in terms of the bond, quite clearly, an element of the refinancing was opportunistic. You know, the market, the interest rates are very low. And therefore, when we look at our debt maturity profile and the market, we felt it was a good time to execute the strategy of diversifying our sources of funding.

Because as you said quite rightly, we relied historically on bank loans and the profile was skewed to that. So we were opportunistic, in terms of benefitting from a positive market environment. And therefore, we have a more diversified source of funds, which gives us the ability to execute, you know, our strategy.

Tom Jones: That's very helpful. I'll get back in the queue.

Anne-Françoise Nesmes: Thank you, Tom.

Operator: Thank you. The next question comes from the line of Kyle Rose from Canaccord. Please ask your question.

Kyle Rose (Canaccord Genuity): Great. Thank you for taking the questions. Two from me.

The first, I just wanted to see if you could give us a little more information regarding the Integra acquisition. I guess, you know, why was that the right mix of assets, you know, now? And then, how do you think about the opportunity with respect to future M&A? You know, should we expect more tuck-ins of a similar size or do you have any appetite to maybe take a bigger play?

And then, secondarily, on the US market, specifically as it stands in Wound Care. If I remember correctly, you know, you highlighted, you know, some positive contract wins on the AWD side, I think, about this time last year. Have we started to see those impacts in the US? And then, how should we think about the bioactive business, given you've got the sales force fully trained and engaged? How should the US Wound Care business broadly, you know, trend as we think about exiting 2020 and into 2021? Thank you.

Roland Diggelmann: Thank you, Kyle. Thanks for the questions. On Integra, I think you probably heard me earlier, or in the past as well, talk about complementing our strong Reconstruction business with upper extremities and notably with the shoulder. So we've been looking at the market for some time.

We always felt this would be very complementary to the portfolio. And I'm very excited about the development that's underway for a new shoulder system, stemless, and with various options. So we felt that was the appropriate time. We pushed it through despite the current challenges, but we feel very comfortable with this.

It also gives us a play – an additional play in foot and ankle, which is great. And with that, it strengthens the commercial capabilities also not just with the Joint team, but also with the Trauma team. So, I believe we have opportunities there.

We acquired a full commercial sales force in the US, and then we have some distributors in Europe, and then in the rest of the world that also, I believe, we can leverage better in-house. So we feel very good about this acquisition, both strategically and in the current timeframe.

On US Wound Care, indeed, some wins, which have taken and will take a bit longer to materialise because of the current environment, as you would expect. But I feel very comfortable here. I think we'll have a good fourth quarter in AWM, overall, and that will also be owing to some improvements in bioactives.

As you mentioned, we now have a fully trained sales force on both ends. You know, the Smith & Nephew and the prior Osiris have been cross-trained and we have the ability to sell bioactives now across. And I think that will help us. We also have – on the regulatory and the reimbursement front on the – in the US, we will see some support for that.

Kyle Rose: Thank you for taking the question.

Roland Diggelmann: Thank you, Kyle.

Operator: Thank you. The next question comes from the line of David Adlington from JP Morgan. Please ask your question.

David Adlington (JP Morgan Cazenove): Good morning, guys. Thanks for the questions. So two, please.

So firstly, just on Wound. You've had a couple of peers reports that have sort of come in slightly better, in terms of growth. I just wondered if you thought you are losing share or if there was anything, with respect to maybe your geographic mix, is impacting your growth on the Wound Care side?

And then, secondly, just in terms of margins for the full year. Obviously, you've pulled out the transactional impact from foreign exchange. Maybe if you could just expand a little further on that and how we should be thinking about revenues and cost evolution through the second half, you know, for full-year margins? Thanks.

Roland Diggelmann: Thank you. We don't typically comment on the margins on the third quarter. So we will try to give you a little colour, but maybe Anne-Françoise can give you some general comments there.

The first one on Wound. Absolutely, we have a different mix. We have a strong business in Europe, which has been more affected by COVID, as you all know. And I think that's one reason to bear in mind. We have seen some softness in Asia. Some of that related to staffing patterns.

I don't feel, at this stage, that we have enough data to say whether this has had an impact on market share. I think we're well-positioned. But the access to healthcare facilities over the – during the COVID crisis, of course, remained challenging in some – especially in some markets. And then, of course, in Devices, we also, of course, see an impact from the lower number of elective surgeries.

Anne-Françoise Nesmes: So I'll take the question then, Roland, around margin, to the extent. What I'll first say, I remind you around the cost savings we've put in place to mitigate the impact of COVID-19. And we've had – we had talked about and we indicated in May that we were targeting up to $200 million of savings in discretionary costs for the full year in 2020 versus our expectations or budget.

We have - we are delivering on that. We are delivering this target. And really, it was in areas, you know, around variable pay, third-party commissions, travel, consultancy. So some of that, you know, was directly linked to activities. And therefore, I would point out as well you should not consider the savings as being structural in nature, as you look at 2021. So that's in play and that's certainly being realised.

And then, the other element you need to think about for the full year is the transactional FX, which you mentioned yourself, and, of course, some negative operating leverage from the fact that the volumes are reduced. But that – just as well, if I may, since I'm on the topic of margin, I think it's important, you know, over time to focus on volume and the revenue growth.

You know, we will look at efficiencies. We'll continue to be as efficient and drive for efficiencies. But the margin will move as we drive volume growth. And therefore, the strategic topics that Roland has covered are very critical, are important, in terms of, you know, driving margin.

Kyle Rose: Okay, thanks.

Operator: Thank you. The next question comes from the line of Veronika Dubajova from Goldman Sachs. Please ask your question

Veronika Dubajova (Goldman Sachs International): Yes, good morning. And thank you for taking my questions, please.

My first one is sort of a follow-up on the question that David's just asked around margins. I think, Anne-Françoise, your predecessor talked about, from memory, I think 50 basis points of transactional FX impact. If you can just quickly clarify whether that number is the same or if it's changed and if you have any insights into what it might look like in 2021? I think you alluded to maybe that – there being some continuation as we moved into 2021. That would very much help us with our modelling.

And my second question is a big picture question for Roland. Obviously, I appreciate we are living in a very uncertain environment and I think you made in your prepared remarks, the statement that you think COVID will probably be here through at least first half of 2021. I guess I'm just curious, in that context, how you're thinking about the Group's ability to return to positive organic revenue growth? And you know, what do you think – you know, when might that come in your mind? Is that really a second-half 2021 event or might that happen sooner?

I mean, I guess the comps in the first half will be very easy, but just kind of curious how you're thinking about that. And two, just, you know, what do you think you need to see to get to that, you know, sustainable positive organic revenue growth and, I guess, revenues getting above the state where it's above the level where they were in 2019?

Anne-Françoise Nesmes: So whilst Roland thinks about the more forward-looking question, I'll pick up the forex. You'll be glad to know there is consistency with my predecessor. I know normally, a CFO comes in and everything is new and changing. But here, we'll be very consistent.

You're right to say, Veronika, that the forex is about 50 basis points in 2020 and we expect the same roughly in 2021. So, Roland?

Roland Diggelmann: Hi, Veronika. On the growth, of course, on the return to growth, I think that's, of course, the big question that we're all asking here. What we see, of course, is a continued impact of COVID. We have limited visibility, like everyone else, as to how long this will go.

We're seeing very different guidance in the recovery. We're seeing, overall, I think, a very strong resilience in this industry, overall, when you look at elective surgeries, when you look at a return to activity levels in Sports Med and Wound, in general. So I'm generally optimistic. I don't have this – I don't know how long the current crisis will continue. Clearly, it will be different in different parts of the world and we've seen that.

What we've also learned, I think, through the first wave is clearly that we have now, as all stakeholders – and I'm talking politics, society at large, healthcare systems, healthcare delivery, and also on industry – and I think we've learned a great deal on how to manage parts of that crisis. I don't expect the same level of shutdowns and restrictions.

And I also think we have very good protocols across the board now in place that really aim at one thing, that's providing patients with the care that they need. And that care, as you know, the fundamentals are there. They'll continue to be strong. They are supported by the global, you know, demographic trends: more aging population that needs more care, more access to healthcare facilities, and healthcare, in general, in Emerging markets.

So – and I think the fundamentals are very good. And I would expect us to be able to return to growth that exceeds 2019 as soon as the COVID restrictions or as soon as we have the ability to fully manage the COVID impact.

I look at – back in the second quarter and third quarter. We did grow despite some challenges in the US, in China, in Germany. And that fuels my optimism that despite the challenges, as an industry, but also at Smith & Nephew, we have taken the right learnings and we are able to grow in these circumstances.

Veronika Dubajova: That's very helpful. Thank you, Roland. And thank you, Anne-Françoise for your answers as well. And thanks – nice to meet you over the phone.

Just a quick follow-up, if I can, Roland. One of your peers has been very optimistic about the backlog. And they sort of quantified what they think is, you know, the backlog of cancelled delayed surgeries, patients in pain. What are you views on that? Do you share that optimism?

And have you guys done any work on – you know, when do you think we might get that vaccine? Is there – what's the sort of bolus of demand that might appear once we get it or do you think that's not how it will play out? And I'll go back into the queue with that. Thank you, guys.

Roland Diggelmann: Thanks, Veronika. Yeah. Of course, we're – as you can imagine, we're running multiple scenarios. The challenge with those is, of course, we don't have the full visibility. So we have the scenarios in the drawers and know what they could lead to, but I just can't give you any numbers or data here because we just – like everybody else, we don't have the visibility.

Now, specific to the backlog, absolutely, we've seen that. It's not a uniform pattern that we see. But of course, you have – especially in the private healthcare system, you build backlogs quicker and they'll be worked on faster. So those are the markets that actually responded and recovered fastest.

And then, again, the question that we were talking with our customers becomes what is backlog? What is really, you know, organic growth? And what's the mix and over what period of time can you address that?

Clearly, what we're seeing in other healthcare systems, which are more public-driven, is the build-up of waiting lists. This is something that I think, in the system inherent, is unavoidable. We don't like to see this. But at the same time, what it also gives you is this – the certainty that, of course, you're going to continue to see ongoing demand because that waiting list will have to be worked over, sometimes, pretty long periods of times.

So it's a very mixed picture. I'm afraid I can't give you the – this crystal ball view that we all would like to have.

Operator: Thank you. The next question comes from the line of Lisa Clive from Bernstein. Please ask your question. Lisa, your line is open.

Lisa Clive (Bernstein): Oh, apologies. Just as we think about – could you maybe comment a bit on the competitive dynamics in the negative pressure market? And two-folds, one, how you've been progressing in continuing to increase your penetration on the hospital base through traditional negative pressure? And also, number two, whether you've seen any competitive threats from the Combitech products that launched a while back?

Roland Diggelmann: Certainly. Thank you, Lisa. We believe that we're very well-positioned in this marketplace. We believe that with PICO, we have really a very, very strong product. We have continued to invest in it. We will have the next generation of PICO coming in late '21. We entered this crisis with the Devices growing at double-digits. We were very confident that under normal circumstances, we can carry that rate forward.

Yes, of course, there is competition. I don't view this as a huge threat. We have good information on our product, what it does. We have the performance data. We have, in some cases, you know, very specific clinical data that point to the effectiveness, the superiority of PICO. So that's what we'll continue to do is, is invest in value-based offerings, document what we do in the clinical setting. And I feel really, really strong about our PICO franchise.

Lisa Clive: And then, within the hospital setting, you know, you obviously lost some momentum several years back when the products had to be withdrawn for a little bit due to some issues around FDA approval of an update. How has that progressed, in terms of regaining market share?

Roland Diggelmann: Yeah, you're absolutely right. I mean, I think it's about regaining market share. I think it's both an opportunity for the hospital setting and the home health setting. In the hospitals, RENASYS was actually growing double-digit pre-COVID. So we feel that we've regained some momentum and that we have put ourselves in a position to actually capture market share again.

Lisa Clive: Thank you very much.

Operator: Thank you. The next question comes from the line of Oliver Metzger from Commerzbank. Please ask your question.

Oliver Metzger (Commerzbank AG): Yeah, hi. Thanks a lot for taking my questions.

The first one is on the recovery in Hip Implants. Could you give us any idea what part of this increase was related to pent-up demand versus underlying development?

My second question is on Integra. So can you also give us some indication how Integra has performed over last nine months now, excluding the negative impact related to the corona pandemic? So all the potential results has shown a higher resilience to your core business. Thank you

Roland Diggelmann: Thank you, Oliver. On the first one, on the Hip side, I think we've seen really good growth. It's really difficult to say whether that was pent-up or just organic. I think for the most part of it, it is a mix.

We are seeing that hips are being performed quicker by – than knees, in general. And I think with the OR3O, we really had a very strong launch and some pull-through effect on the rest of the Hip franchise as well. And then, of course, hip surgery is also more prone to trauma, especially in the elder population. So that certainly also helps, in that context.

On the Integra data, I'll have to come back to you. I don't have those on top of my mind. What I know anecdotally is, of course, that there has been an impact, just like for everybody in the industry as well, on the Integra Extremities franchise. But I don't have that number. I'll get – we'll get back to you, if that's okay, Oliver.

Oliver Metzger: Okay, great.

Anne-Françoise Nesmes: But just as a reminder –

Oliver Metzger: Thank you.

Anne-Françoise Nesmes: Just as a reminder, Oliver, to just give some sort of value [?] context, we did put in the announcement that Integra generated $90 million of revenue in 2019 and traded a small lot. But they are reporting soon as well. So you'll get their data.

Oliver Metzger: Okay, great. Thank you.

Operator: Thank you. The next question comes from the line of Chris Gretler from Credit Suisse. Please ask your question.

Christoph Gretler (Crédit Suisse): Yeah. Thank you, operator. Good morning, Roland. And welcome, Anne-Françoise. I have two questions.

And the first also relates to Integra. Actually, could you provide a sales split into lower and upper extremities for that business? And I noticed now, it's a relatively small market share there – that you are buying there. Is there any appetite, you know, to grow that business and, you know – there your relative market position, you know, via acquisition further on or is this basically kind of the beachhead you have, you know, to necessary – the beachhead, you know, necessary to grow organically? So that will be the first question.

The second question, maybe just on October trading, you know? If you maybe have, you know, some indication about, you know, the trends that you have seen just as of late, you know? And I was a bit surprised that, you know, kind of, you know, the three months, you know, in Q3 were kind of, you know, fairly stable. So I was just wondering, you know, kind of whether you had, you know, a bit more of an indication for us, you know, how now things are doing on a run rate basis? Thank you.

Roland Diggelmann: Thank you, Chris, for the questions. On Integra, firstly, I'm afraid we are not giving breakdowns at this stage. We may, as we go further and we fully integrate the business. But from a business and strategic perspective, I think what it gives us is access to the shoulder market for the Recon business. It gives us access to foot and ankle and other extremities, also in the trauma business. So it's a great complementary business.

It gives us a sales force that is dedicated and has access to specialists. It also gives us a crossover into sports med, when you think about pure shoulder specialists that would do any surgery that is relative to shoulders. So there, we can bridge nicely from sports med across the entire continuum and, if necessary, into the recon side of it. So that's really attractive.

We continue to look at the market, of course, opportunistically. But right now, with what we're going to be bringing in-house with Integra, I feel very good about our ability to play in this faster growing market of extremities and of shoulders, in particular.

And then, I'm very excited about the development that's under way with the great surgeon group for a new shoulder design, stemless, state-of-the-art that will come to the market in '22. So that will need a little bit of patience. But the state of the development there is well-advanced.

On October trading, we typically don't comment on individual months. But I would say, you know, it's been there – I would say, a continuation at this stage. But remember, month-to-month variation is going to be pretty heavy. And then, we're still not end – at the end of the month. So typically, we have quite a lot of activities towards month-end.

What we certainly also see now is more restrictions being applied in Europe, in particular. I am hopeful that they will not impact elective surgery, overall, at a large degree. But we will see, again, different restrictions being imposed. I believe that in Switzerland, in Germany, there is a great ambition to continue with elective surgeries, also on the basis of the learnings from the first wave. Whereas in other countries, like Belgium, all elective surgeries have now just been suspended. But this information is just coming over the last few days. So you see that the situation is very fluid.

And then, I wouldn't read too much in individual months. Same, by the way, holds true for Quarter Three because there, we have some very weak months, typically, as comparators with the summer months and the breaks. And this year, everything was a bit different, in terms of the pattern and the rhythm. So we'll know more at the end of the year when we really have the full fourth quarter under our belt. And of course, we will know more about the ongoing COVID-19 situation.

Christoph Gretler: Okay. Thank you very much for your comments here.

Roland Diggelmann: Thanks, Chris.

Operator: Thank you. The next question comes from the line of Michael Jungling from Morgan Stanley. Please ask your question.

Michael Jungling (Morgan Stanley): Great. Thank you. And good morning, all. I had – I have three questions.

Firstly, on sales force. Can you talk about the sales force turnover in each of your three franchises since COVID hit you in Q1 and Q2 of this year?

Question number two is also on sales force. What do you expect will happen to your sale force stability over the next six months, with a view perhaps that these sales reps have mouths to feed and are looking for a more stable healthcare area?

And then, finally, also on sales force. Can you please update me on the split now that you have for Ortho and Sports Medicine between your own sales force and how much goes through distributor sales forces? Thank you.

Roland Diggelmann: Good morning, Michael. Thanks for the questions.

Yes, of course, sales force is very, very important to us. I am pleased to report that we have not had any layoffs nor furloughing, as a matter of fact, in the organisation. We took that decision very early in the crisis. And of course, that was, then, to protect our sales force and to protect the strength of the organisation.

Since, the attrition rate is well below last year's, as one would expect. But we've also taken many other measures in protecting our sales force, especially around the US, where it's a heavy commission-based sales force where, in some cases, we had advanced the commissions. We have ensured that, you know, even though the activity level dropped massively, that those people remain with us. And I'm very confident that they will also remain with us in the future.

First of all, as we continue to see the recovery, they will see, you know, there is great opportunities for them. At the same time, I think there is – obviously, we did a lot, as a company, to support our sales force. Thirdly, these are specialists. It's not that easy for them to shift from one to the other industry. So I think that's quite inherent.

Now, on the third question between direct and indirect. We have made a couple of deals, brought distributors in-house, strengthening the direct sales. Especially in the US we continue to look for opportunities. Also, in other markets, some of the plans have been put on hold for now. But we'll continue to push to be more direct as we prefer, of course, to have the margin to the end user and have direct contact with our customers.

Now, the breakdown, specifically, I don't think we have been disclosing that. We might come back on that at a later stage. But I wouldn't want to give you any number at this stage.

Michael Jungling: Okay. And then, finally, Roland, I think when these furloughing schemes were available earlier this year – I think I asked you this maybe in Q1 or the Q2 earnings call – I think you were reluctant to take on any benefits. If – will this change, this time around? If COVID gets worse, are you willing to take on government support schemes?

Roland Diggelmann: We would have to look at it on a case-by-case situation. Generally, I am not really a fan of this because it always puts you in a certain situation where you are indebted or you owe something. So that was an easy decision early on. I don't expect the second wave, or whatever we call it, to be as heavy or as dramatic than the first wave. So that question probably, or hopefully, won't come up.

But my position remains the same. We protect our organisation. We don't layoff for COVID because we need each and every one for the recovery. Because the fundamentals in the business are sound and we'll continue to see, you know, growth in number of procedures in the future. And we don't want to be dependent on government aid. So that's been my position. I don't see that changing in these circumstances.

Michael Jungling: Thank you.

Roland Diggelmann: Thanks, Michael.

Operator: Thank you. The next question comes from the line of Julien Dormois from Exane. Please ask your question.

Julien Dormois (Exane BNP Paribas): Hello. Good morning, Ronald. And *bonjour* and *bienvenu*, Anne-Françoise. I have two questions.

One is on the US, especially the hospital groups, the hospital systems in the US, which have started to reduce CAPEX pretty heavily in Q2 and Q3 and which are obviously focussed on protecting their cash flow, given the context. Do you see that as a hurdle when it comes to the launch of CORI right now? And second leg of the question is, have you started to see some of your customers initiating discussion regarding some price concession on the device side of things?

And the second question is a broader one, which is on the cost side of things. If and when we get into a world post-COVID, do you see an opportunity for some structural cost savings maybe in terms of maybe less travelling, or maybe more remote, or digital promotional activities – anything like this that you would start working on?

Roland Diggelmann: Hi, Julien. Thanks for the questions. You know, regarding the first question on capital spend, I think, indeed, there was – obviously, at the height of the crisis, there was some caution around capital spend. I think – I haven't come across any cancellations. It was more rather deferrals. Remember, these hospital groups are very competitive. They mostly cater to the private markets. They want to have the latest in technology. And with that, I do expect capital sales to take up again.

CORI, in particular, I think we're very well-positioned because we have a very differentiated solution which has a much smaller footprint. It's lighter. It's more mobile. And with that, we believe we also have a much better cost base. And so, I don't think that we'll see a negative impact. On the contrary, I think we could actually see a positive, also with regards to – in ASCs and the growth and, actually, the readiness of CORI for ASCs.

On the pricing side, it's been remarkably quiet so far. I haven't heard much on this side. I think this will all come with a certain delay. I think everybody is right now – continues to be focussed on managing through the crisis. There has been some inconsistencies here and there, but nothing that would have been systemic.

And then, on the cost – and Anne-Françoise, please chip in – I think, obviously, we've engaged with customers definitely much more through digital means, different technologies, medical education, big convention and events, and travel has all been impacted. And in every crisis, you have opportunities. We've got to build on that.

We have trained, I think, more than 20,000 physicians online through new means. This is certainly something that will stay, that we'll continue to build on. We see more opportunities in end-to-end solutions with, indeed, digital tools, whether that's around identifying the right patients for ASCs and managing through the reimbursement or accompanying the patients, pre and post-surgery, through also digital solutions.

So there is a lot that will, you know, probably be accelerated and amplified through this crisis. And then, of course, there are some areas where, potentially, we'll see lower cost of travel maybe, of large conventions, of large meetings. That's certainly a possibility.

Anne-Françoise Nesmes: So *bonjour*, Julien. But I guess I'll pick up the answer in English.

Just to add to what Roland said is, you know, most of the savings we've achieved are variable costs. They are not structural in nature. And therefore, it will be our decision, our choice to then balance cost control with our ability to take part in the recovery of the market and reinvesting. And while some activities will change in shape, you know, we are quite clearly balancing that recovery and cost control to make sure we can grow and recover.

Julien Dormois: Okay, thank you. *Merci beaucoup*.

Operator: Thank you. The next question comes from the line of Kit Lee from Jefferies. Please ask your question.

Kit Lee (Jefferies): Thank you. Two questions for me, please.

I think firstly just on France and Germany. You mentioned that the markets have returned to growth in Q3. But have you seen a softer recovery just towards the end of the quarter, just given the rising infection rates, or is it not the – is this not the case?

And then, my second question is on the Advanced Wound Care business. Can you just split the performance between the surgery and community channel – you know, whether one is growing faster than the other or are you seeing more pressure in one channel compared to the other? Thank you.

Roland Diggelmann: Thanks for the questions, Kit. I didn't quite get the second one. So I'll answer the first one and then maybe we can get back to that second question.

So Germany and France, we've seen good recovery through the quarter. That was really encouraging. And we didn't actually see a softening later in the quarter. I think this actually continued to perform well.

What we now have, of course, is a slightly new situation with the latest announcements made as late as yesterday in both France and Germany with further – I would say, further measures to contain COVID, which, we believe, will, in some form, have an impact on, of course, elective surgery as well and possibly also on activity-based surgeries.

Now, how much that will be, we don't know at this stage. As I mentioned, I think, these countries have also learned and they have also an ambition to continue to deliver care to their population beyond just looking after COVID-19 patients. And I think that's something that we've also experienced on the positive side. But what the impact will be, we don't know.

At this stage, the situation is fluid. We're observing it. We have our people on the ground very close to our customers. And we certainly will be able to react again as we've had – as we've done in the very recent past.

I can see here – my team is helping me. The question was around AWC and the relative growth between hospital and community channels. Is that your question, Kit?

Kit Lee: Yes, that's right.

Roland Diggelmann: Okay. I'm afraid I don't have the data here. We'd have to come back. Sorry about that. I don't have that number globally.

Kit Lee: Okay, thank you.

Roland Diggelmann: Thank you, Kit.

Operator: Thank you. There are no further questions. I would like now to hand the conference over to Roland Diggelmann for closing remarks. Please go ahead.

Roland Diggelmann: Thank you, Nadia. And thank you, everybody, for taking the time. I wish you all the best, and a good fourth quarter to all of us. Thank you.

Anne-Françoise Nesmes: Thank you.

Operator: That does conclude our conference for today. Thank you for participating. You may all disconnect. Have a nice day.

[END OF TRANSCRIPT]