
2004 active lifestyles demand the wright approach
WRIGHT.

"I am so thankful for my new lease on life.

I feared that my future would be one of watching; not doing.

But I can once again do activities normally taken for granted."

Donna Diamond, 36-year-old
CONSERVE® BFH™ Hip Recipient

the wright approach
leads to the right results for patients

Walking, yoga and skiing are just a few of the activities women in their thirties can enjoy in their free time. They certainly don't think twice about everyday activities like jogging up a flight of stairs to grab the phone.

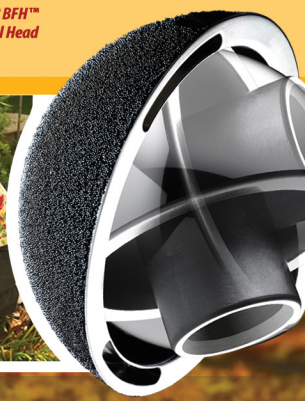
For 36-year-old Donna Diamond – and others who suffer from chronic joint pain – this couldn't be further from the truth. Donna was born with a dislocated hip. While she learned to walk normally, she was advised by physicians to refrain from high impact activities.

Physicians told Donna to "hold off as long as you can" on total hip replacement surgery because the implants currently available only lasted about 10 years. For a woman Donna's age, this would mean she would face multiple revision surgeries throughout her lifetime. Doctors advised "we can only do so many surgeries before you would eventually be in a wheelchair." Donna held off as long as she could by taking pain killers and refraining from activities she loved, but the situation grew steadily worse. **"I couldn't sleep through the night because of tremendous pain. I felt like a young woman trapped in an elderly woman's body."**

In early 2004, Donna saw Dr. Steven Gitelis at Rush Presbyterian Hospital in Chicago. He suggested a new total hip replacement, Wright's CONSERVE® Total Hip with BFH™ Technology. The hip is designed to reduce the risk of dislocation and to mimic the natural kinematics of the hip. The femur's head is replaced with a larger diameter femoral head than conventional implants for improved range of motion. Best of all, physicians believe this type of implant can last much longer than the 10-12 years of traditional hips, perhaps up to 30. This was terrific news for 36-year-old Donna.

Donna was implanted with the CONSERVE® BFH™ Hip in March of 2004 and she recovered quickly. Today, you will find Donna participating in hobbies such as gardening, and enjoying an active life again.

the CONSERVE® BFH™
Acetabular Cup & Femoral Head



the wright approach to MARKET SEGMENT		KEY SOLUTIONS
biologic solutions		Bone Repair Infection Treatment Soft-Tissue Repair Anti-Adhesion
extremity solutions		Foot & Ankle Hand & Wrist Upper Extremity
hip solutions		Advanced Bearing Surfaces Bone Conserving Implants Modular Necks MIS Techniques – Hips
knee solutions		True Anatomic Kinematics MIS Techniques – Knees Limb Salvage

what is the wright approach?

For more than 50 years, surgeons and patients have come to depend on the "Wright Approach" — a philosophy that combines innovation, passion and people for life-changing results. **The Wright Approach is a pioneering spirit** that both drives our Company and provides focus for navigating the opportunities and challenges of the orthopaedic industry.

The Wright Approach is built on innovation. Simply following the lead of others is not an acceptable course. We take the helm of invention by staying attuned to the challenges and needs of surgeons and patients, and responding with solutions that reshape the thinking of our industry.

WORLDWIDE MARKET	GROWTH	% of TOTAL REVENUE
$750 Million	Market Growth – 36% Sales Growth – 24%	20.9% 
$317 Million	Market Growth – 12% Sales Growth – 14%	12.2% 
$3.7 Billion	Market Growth – 18% Sales Growth – 27%	33.3% 
$4.0 Billion	Market Growth – 16% Sales Growth – 12%	29.4% 

The Wright Approach is fueled by passion. Innovation without passion is an empty endeavor. But when the journey toward a unique resolution is driven by an intense appetite for discovery, the results can astound.

The Wright Approach values people. We depend on the unique contributions and dedication of over 850 employees worldwide to breathe life into the Company's body of sound objectives.

The Wright Approach is what led our Company's founder, Frank O. Wright, to take one unique orthopaedic invention and plant the seeds for a global corporation that today designs, manufactures and markets over 40,000 reconstructive joint devices and biologic materials. Likewise, it is the compass by which Wright Medical Group will lead the way into and navigate the future of orthopaedics. Headquartered in Arlington, Tennessee, the Company participates in the $19 billion worldwide orthopaedic market and distributes its products through a combination of direct sales personnel and a network of independent distributors. Wright's common stock is traded on the Nasdaq National Market under the symbol "WMGI".

. . . and for shareholders

financial highlights (in thousands, except per share data)

	2000 [1]	2001 [2]	2002 [3]	2003 [4]	2004 [5]
NET SALES	$157,552	172,921	200,873	248,932	**$297,539**
GROSS PROFIT, As Reported	$77,182	121,570	145,257	181,117	**$213,356**
(as a percentage of net sales)	49.0%	70.3%	72.3%	72.8%	71.7%
GROSS PROFIT, As Adjusted	$106,263	121,570	145,257	181,117	**$215,875**
(as a percentage of net sales)	67.4%	70.3%	72.3%	72.8%	72.6%
OPERATING INCOME (LOSS), As Reported	$(24,636)	8,561	26,555	27,166	**$38,413**
(as a percentage of net sales)	(15.6%)	5.0%	13.2%	10.9%	12.9%
OPERATING INCOME, As Adjusted	$4,465	8,561	21,555	31,724	**$42,095**
(as a percentage of net sales)	2.8%	5.0%	10.7%	12.7%	14.1%
NET INCOME (LOSS), As Reported	$(39,493)	(1,507)	25,060	17,397	**$24,022**
(as a percentage of net sales)	(25.1%)	(0.9%)	12.5%	7.0%	8.1%
NET INCOME (LOSS), As Adjusted	$(10,412)	(1,507)	16,398	20,216	**$26,451**
(as a percentage of net sales)	(6.6%)	(0.9%)	8.2%	8.1%	8.9%
DILUTED EARNINGS (LOSS) PER SHARE, [pro forma] [6]					
As Reported	$(2.29)	(0.06)	0.75	0.50	$0.68
As Adjusted	$(0.60)	(0.60)	0.49	0.58	$0.75
TOTAL ASSETS	$216,964	193,719	276,370	322,103	**$361,158**
TOTAL LONG-TERM OBLIGATIONS	$112,283	19,804	16,586	11,096	**$5,952**

(1) 2000 adjusted results presented above exclude the unfavorable effect of a $29.1 million noncash charge to cost of sales for inventory step-ups recorded pursuant to APB No. 16 in connection with the Company's recapitalization and acquisition of Cremascoli.

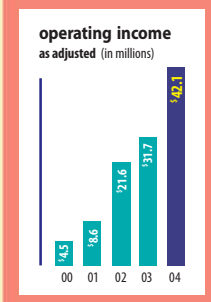
(2) In accordance with the provisions of SFAS No. 145, "Recession of FASB Statements No. 4, 44, and 64, Amendment of FASB Statement No. 13, and Technical Corrections", the Company's $1.6 million loss on early retirement of debt in 2001 does not meet the criteria to be classified as extraordinary. Consequently, pursuant to this newly adopted standard, this amount has been reclassified and included in the Company's results from operations.

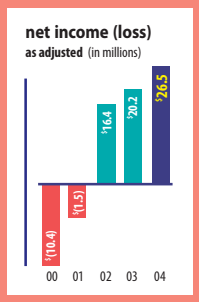
(3) 2002 adjusted results presented above exclude the $4.2 million arbitration settlement award ($2.6 million after tax effect), the $800,000 royalty resolution ($593,000 after tax effect), and the $5.5 million income tax benefit.

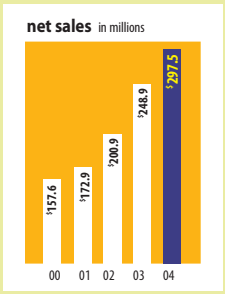
(4) 2003 adjusted results presented above exclude the $4.6 million ($2.8 million after tax effect) acquired in-process research and development costs.

(5) 2004 adjusted results presented above exclude $2.4 million ($1.6 million after tax effect) of costs incurred to write down certain foot and ankle inventory to its net realizable value and $510,000 ($338,000 after tax effect) of accelerated depreciation on surgical instrumentation related to this inventory as a result of the transition of this product line to our CHARLOTTE™ Foot and Ankle System and $791,000 ($511,000 after tax effect) of costs associated with the voluntary market withdrawal of certain CONSERVE® hip components.

(6) The computation of pro forma diluted earnings (loss) per share for 2001 and 2000 includes shares issuable upon the conversion of convertible preferred stock and related dividends as if such stock was converted on January 1, 2001, and 2000, respectively. The computation of pro forma diluted earnings per share for 2004, 2003 & 2002 do not differ from actual per share results.







biologic solutions
such as a novel approach to treating slow-to-heal stress fractures (Jones Fractures) which plague the athletic community
read more ... page 8

extremity solutions
such as a new distal radius product that revolutionizes how the most common fracture is treated
read more ... page 10

hip solutions
such as new hard bearing materials developed for younger, active patients so they no longer have to wait for surgical relief
read more ... page 12

knee solutions
such as minimally-invasive techniques used to speed recovery while restoring natural motion
read more ... page 14

the wright approach
leads to the right results in 2004

To Our Stockholders, Customers and Employees:

For Wright Medical Group, Inc. stockholders, 2004 proved to be another outstanding year. Overall performance reached levels yet unseen in the history of the Company or that of the orthopaedic device industry. Through the Wright approach of well defined objectives and business plans, our surgeons and patients benefited from a wealth of innovative new hip, knee, biologics and extremities products, while stockholders profited from the Company's record financial results. Our steady flow of new product innovations also fueled the broadening of our distribution system, thereby expanding our reach within the orthopaedic market. We anticipate the trend of success to continue as market dynamics remain very favorable for our portfolio of orthopaedic products. In a worldwide orthopaedic market that reached approximately $19 billion dollars in 2004 and continues to grow, we believe Wright is very well positioned to take advantage of opportunities related to our thriving industry. Furthermore, we are committed to making the necessary investments to maintain the momentum we have created over the last five years.

Our growth rate in 2004 continued to be favorably impacted by the success of our reconstructive hip joint implants, specifically the PROFEMUR® modular neck implant line and our high performance ceramic-on-ceramic and Big Femoral Head (BFH™) metal-on-metal hard bearing technologies. Significant investments were made to broaden our hip implant offering with stem designs that suit the preferences of surgeons within the United States. The Company is now benefiting from those new product line investments, attracting larger audiences of hip surgeons to the use of its products.

In 2004, we made additional investments into Wright's reconstructive knee line, specifically, newer tibial component designs that address the cruciate retaining segment of the total knee market. To date, these enhancements to the knee product line have been very well received, strengthening our belief that future knee growth should keep pace with the overall market growth rate.

Our biologics business continued to be a strong catalyst for sales growth in 2004, reaching 24%. Significant investment into higher-performance synthetic bone graft substitutes should enable us to take advantage of several market-defining longer-term opportunities within the trauma and spine segments of orthopaedics in the future. Our extremities business exceeded the overall market growth rates in 2004, with new product introductions during the latter months of the year positioning

Laurence Y. Fairey
President, CEO & Director

F. Barry Bays
Executive Chairman of the Board of Directors

the wright approach to leadership
New President & CEO Shares Vision for the Right Results

On July 1, 2004, Laurence Y. Fairey officially took the reigns as President & CEO of Wright. A native Memphian with 28 years of experience in the orthopaedic industry with companies like Smith & Nephew Richards and Sofamor Danek (now Medtronic Sofamor Danek), Fairey first joined Wright as a member of the Board of Directors in January of 2004. His interest in the company, however, dates back to the earliest days of Wright Medical Group, Inc. when he saw a dramatic turnaround in both performance and confidence taking place at a small orthopaedic company. He knew that something exciting was brewing at Wright – and the company's Board of Directors knew that Fairey could offer expertise in sales, marketing and distribution to lead Wright to new levels of excellence.

"I am here to provide strategies," the new President & CEO explains. Service is a defining element of those strategies, just as it is in Fairey's own leadership style and business philosophy. As Wright's new President & CEO, he shares his passion for service in a way that is transforming for the company and each of its employees. **"Customer service must be routinely refined, and therefore redefined, to distinguish a company from its competitors,"** Fairey stresses. Embracing that notion, he explains, is essential for achieving the right results – for surgeons, patients and shareholders.

us for continued success in 2005.

Our primary growth drivers during 2004 were our reconstructive hip and biologics product lines, while our extremity/small joint implants and reconstructive knees contributed nicely, as well. Our strategy of carefully focusing new product development efforts in high margin, procedure-specific product areas within the orthopaedic market will continue to be our general guiding business strategy into the future. We believe that this approach allows us to be more opportunistic, leading to above-market overall growth rates for the business as proven by the gains the Company made in 2003 and 2004 within the reconstructive hip area. We believe our approach of offering procedure-specific products that clearly distinguish Wright from its competitors provides us with distinct advantages in the marketplace. In 2004, R&D spending reached new levels, totaling $18.4 million. A portion of this investment resulted from additional requirements and needs in our global clinical and regulatory submissions and new clinical trials for longer-term new product opportunities.

Key leadership enhancements played a role in our positive results for the year, as well. In January 2004, Wright's Board of Directors appointed two new members, David D. Stevens, current Chairman and CEO of Accredo Health, Inc. and Laurence Y. Fairey, former executive with Medtronic Sofamor Danek's spine division. In July of 2004, F. Barry Bays relinquished the day-to-day duties as President & Chief Executive Officer and was appointed Executive Chairman of the Board of Directors. The Board of Directors then appointed Laurence Y. Fairey as Wright's new President & Chief Executive Officer, knowing his strong background and working knowledge of the orthopaedic business would uniquely qualify him for this position. Wright's management and Board would like to express their appreciation to James T. Treace, who served as the Chairman of the Board of Directors since December of 1999 and continues to serve as a Director.

the wright approach to financial achievement

Wright achieved another record year of worldwide sales and net income, primarily by improving global distribution and capturing new customer accounts seeking to improve their surgical outcomes with our innovative new products and related techniques.

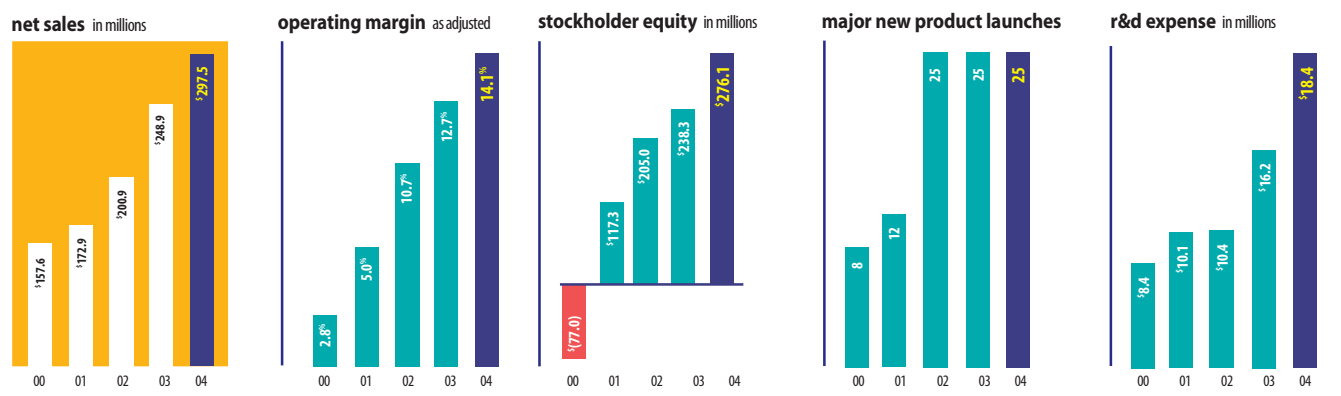
Net sales for 2004 increased 20% to $297.5 million from $248.9 million last year. The Company's net income, as adjusted, for 2004 improved to $26.5 million, or $0.75 per diluted share, compared with 2003 net income, as adjusted, of $20.2 million or $0.58 per diluted share. Our key operating ratios significantly improved during 2004, with operating income, as adjusted, as a percentage of sales increasing to 14.1% from 12.7% in 2003.

Furthermore, our balance sheet saw significant improvement with total shareholders' equity increasing by $37.8 million to $276.1 million at year end, due to the Company's continued positive operating results. We ended the year with a cash balance of $83.5 million and continue to maintain an additional $60 million line of credit.

Overall financial performance was significantly influenced not only by our new product introductions, but also by continued strong performance from our existing core hip and knee reconstructive implants, small joint implants and biologic bone grafting and soft tissue products.

As a result, our domestic business grew at an outstanding 18% over prior year, while our international business grew at 22% over prior year's results. Our worldwide biologics business, consisting of our synthetic and tissue-containing bone graft substitute products, tissue membrane and anti-adhesion products, grew at 24% over prior year's results. In 2004, domestic biologics sales exceeded sales of both our domestic hip and knee product categories for the first time in the company's history. This milestone achievement was due to Wright's approach of ongoing commitment to new product innovation and providing our customers with biologic options that truly represent the cutting-edge technology of this burgeoning market. Families of products that demonstrate this commitment include our unique GRAFTJACKET® Regenerative Tissue products and our MIIG® synthetic bone grafting line, both of which were major growth drivers during the year. Extremities devices including our finger, wrist, elbow, foot and ankle products showed a sound increase of 14% over prior year's results. While this growth rate is somewhat slower than that of prior years, the result is due primarily to launch timing of certain key products that sparked sales activity in the last few months of the year.

the wright results for continued growth



Our reconstructive hip line again demonstrated phenomenal performance in 2004 by increasing 27% over prior year's performance. This result was heavily influenced by the continued customer enthusiasm for the high performance bearing options of our metal-on-metal Big Femoral Head (BFH™) technology and ceramic-on-ceramic acetabular components, coupled with our PROFEMUR® Modular Neck femoral implants. Furthermore, aggressive customer adoption of our ODYSSEY™ Tissue Preserving Initiative for total hip procedures and its procedure-specific instrumentation gave Wright significant exposure within the global orthopaedic community. Exciting growth was also established within our reconstructive knee business, which saw a very nice rebound over 2004, ending the year with an increase of 12%. This improved performance was led by continuing market penetration and growth of our ADVANCE® Medial-Pivot knee system. The launch of this system's new Double-High tibial inserts to address the high flexion and cruciate retaining segments of the total knee market helped to enhance our overall product offering in 2004.

the wright
operating results

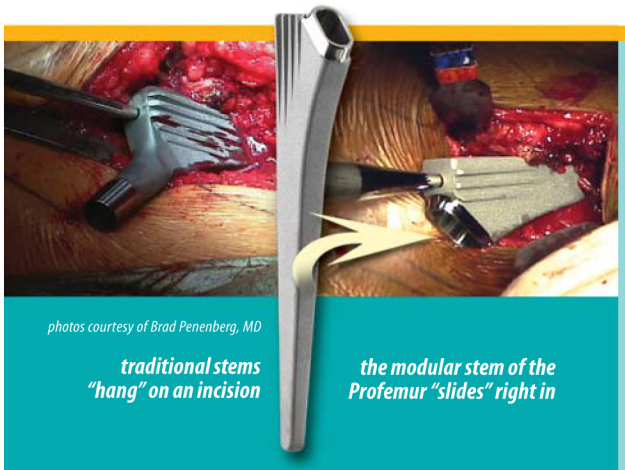
Our financial success in 2004 was consistent with our longer-term financial objective of maintaining low-to mid-teens revenue growth while providing operating results that exceed the revenue growth target. Wright continued to make significant investments into manufacturing equipment, as well as implant and instrument inventory, to support our new product launches. At the same time, the Company continued to leverage its SG&A expenses downward during 2004 to 50.8% of revenues, which is a 0.5 percentage point improvement over 2003 and 4.5 percentage points of cumulative improvement over the last 3 years. Our long-term operating objective is to continue to reduce the overall SG&A percentage by one to one-and-a-half percentage points each calendar year.

Our JD Edwards® business software continues to provide the Company with an advanced global operating system that supports the integration of our international operations. By the end of 2005, Wright is scheduled to have its Japanese operations fully integrated and operational within the JD Edwards® system. Additionally, upgrades in our Cognos® business software, which works in association with our JD Edwards® global system, have enhanced our ability to timely analyze operating results and generate reports to increase visibility and ease of management throughout our global operations.

In 2004, the Company's "lean manufacturing" objectives, coupled with our Six Sigma Quality programs, allowed us to continue revenue growth while significantly reducing the necessary investments in manpower for our global manufacturing operations. Gross margin, as adjusted, remained about the same for 2004 versus 2003. The combination of product mix and more efficient manufacturing operations has continued to keep Wright at or near parity with gross margins of our much larger competitors.

Additionally, 2004 saw the successful completion of the assessment of our system of internal controls that is compliant with the requirements of Rule 404 of the Sarbanes-Oxley Act. At year-end, we received an unqualified opinion from our independent auditors with respect to our internal controls over financial reporting.

Throughout the year, regulatory activities at Wright maintained a steady pace. In 2004, the Company received several key regulatory clearances from the United States Federal Food and Drug Administration (FDA) related to tissue-containing bone graft products. Currently, our entire line of ALLOMATRIX® bone graft products is cleared for commercial distribution, providing Wright a key advantage over our major competitors for these types of biologic products. While the regulatory environment related to tissue-based products will continue to change, we feel Wright is well positioned to adapt to those changes and move forward with many more innovative tissue-based solutions. Wright continues to monitor and comply with all domestic and international standards related to the processing and distribution of human tissue for our bone graft substitute and tissue membrane products. Also in the regulatory realm, Wright worked with the FDA to conduct a limited market withdrawal related to the acetabular hip cup used in conjunction with our CONSERVE® Plus and CONSERVE® Total Hip systems. This voluntary market withdrawal is complete and it appears that the full financial impact was



photos courtesy of Brad Penenberg, MD

traditional stems "hang" on an incision

the modular stem of the Profemur "slides" right in

the wright approach to minimally-invasive surgery

One of the greatest waves of change to roll through the orthopaedic industry in recent years has been the development of numerous minimally-invasive surgical (MIS) techniques for joint replacement. Yet the transition to MIS in joint replacement has faced challenges; including the complexity of many of the new techniques, difficulties with implant positioning, and the risk of soft-tissue damage during the procedure. Responding to these challenges, Wright introduced the ODYSSEY™ Tissue Preserving Initiative in September 2004. **ODYSSEY™ products and processes enable surgeons to confidently and consistently perform MIS procedures without having to radically change the surgical techniques with which they are most familiar.**

In the brief period since its introduction, Wright's ODYSSEY™ Initiative has already provided surgeons with several key MIS advances. The first was a less invasive technique and instrumentation for the Company's PROFEMUR® Hip System with modular neck technology, which is the only hip system in the industry specially suited for a minimally invasive surgical approach. The program was then expanded to include a new, tapered stem design, followed by an innovative technique and instrumentation for less invasive total knee procedures with the ADVANCE® Total Knee System. Most recently, the Company introduced the less invasive PATH™ approach to total hip arthroplasty.

The ODYSSEY™ program illustrates that Wright is not only committed to providing new surgical solutions in this area, but to leading the industry in a new era of minimally-invasive innovation.

captured in a third quarter special charge. With product replacement and retrieval activities behind us, we believe that this matter has been resolved.

the wright approach to new products & market opportunities

A steady flow of new products once again played a significant role in the Company's revenue growth for 2004. Procedure-specific products, coupled with innovative surgical techniques, provided a very positive outcome for patients and surgeons — and resulted in Wright's well-deserved recognition within the orthopaedic community. In 2004, a total of $18.4 million was invested into R&D, representing a $2.3 million increase over 2003 levels. One result of this investment was additional personnel to support regulatory submissions, clinical monitoring and timely global product filings. The industry has seen an increase in the documentation required not only by the FDA, but by all other international regulatory agencies, as well. At Wright, the number of engineering and regulatory professionals addressing these growing annual demands now exceeds 85 individuals.

Knowing the demand for innovation within our industry, we strive to provide our sales professionals and customers three to five major product launches each quarter. To support this aggressive level of new product introductions and address our annual marketing and sales plans, Wright increased its domestic sales force by over 6% in 2004, yielding 318 exclusive distributor/sales persons in the U.S. With many of our new product activities taking place in the biologic and small joint business, we will continue to diversify our domestic distribution system by adding specialists to address opportunities in these areas.

As our reconstructive hip joint business continued to gain positive recognition with hip surgeons around the world in 2004, our hip product line established a number of new milestones. At the top of the list is a worldwide year-over-year increase in hip revenue performance of 27% globally and 33% domestically — placing us among the best of our major competitors. A key contributor to these results has been our ODYSSEY™ Tissue Preserving Initiative. The program features procedure-specific implants and instrumentation, as well as Company-sponsored teaching seminars for surgeons, illustrating first-hand how the ODYSSEY™ approach provides them maximum flexibility in treating a wide range of patients. Through the ODYSSEY™ Initiative, we believe Wright has one of the broadest and most complete product offerings for the ever-expanding minimally invasive hip procedure market, regardless of incision size or number.

Another contributor to our outstanding results in our hip sales was our high performance bearing options, specifically in our LINEAGE® ceramic-on-ceramic hip cup liner and femoral head and our BFH™ metal-on-metal articulating system. Both options offer our surgeons the most advanced high performance bearings. Our BFH™ technology also features a design to enhance range of motion and address the needs of patients who may be more prone to early dislocation following surgery. Furthering the concept of meeting a variety of surgical needs, Wright's PROFEMUR® Modular Neck System directly addresses the requirements of surgeons seeking a minimally invasive hip procedure with maximum flexibility in stem selection, uniform anatomic fit and superior ceramic-on-ceramic or metal-on-metal bearing options. By combining our high performance bearing surfaces with the industry's premier modular neck system, Wright provides a very compelling hip product offering for all surgeons.

Beyond 2004, we hope to expand our compelling hip product portfolio by gaining FDA clearance for our CONSERVE® Plus Resurfacing System. This product offers an alternative to the traditional total hip stem and cup system and may address as much as 10-20% of the overall total hip market. Our CONSERVE® Plus system is designed for the numerous patients who have good bone quality, but suffer from articular deterioration. This type of patient can often benefit from a resurfacing device versus a conventional total hip system that would require removal of healthy bone. A resurfacing implant typically addresses a younger patient population, but can be utilized in a wide range of patients with good bone quality. We feel strongly about this technology and the positive results it can provide for many patients. Since our initial regulatory submission in late fall of 2003, we have been working diligently with the FDA to make this product commercially available in the United States.

Our reconstructive knee business continued to make progress in 2004 with global sales growth of 11.6%, which was in line with the procedure growth rates. Our introduction of the ADVANCE® Double-High tibial component, as well as a renewed marketing approach to reach a broader surgeon base, represented key elements of growth in 2004 and will continue to be key for future growth. The Double-High tibial component significantly complements our ADVANCE® Medial Pivot Knee system by allowing surgeons to more readily address what is known as the "cruciate retaining" and "high flexion" segments of the total knee market. Furthermore, our ODYSSEY™ Tissue Preserving Initiative is also enhancing our knee business. Through the initiative, Wright is providing surgeons with unique procedure-specific instrumentation to perform "mini-incision" total knee surgery. The success-to-date with this program has been encouraging. Throughout 2005, additional surgeon training will continue to ensure that Wright stays at the forefront in this emerging era of "mini-incision" total knee procedures.

Another strong contributor to our positive sales results in 2004 was our biologics line, growing at 24% on a worldwide basis. Growth within this product line was significantly influenced by the GRAFTJACKET® Tissue Membrane and MIIG® Synthetic Calcium Sulfate product offerings. The Company is currently one of only two major suppliers of FDA-cleared tissue-containing bone graft substitutes (the ALLOMATRIX® family of products). Additionally, our core ALLOMATRIX® line of bone grafting products continues to provide a very strong base for the business. Furthermore, in late 2004, the Company received regulatory clearance to market the next generation of our ALLOMATRIX® bone graft substitute family of products. ALLOMATRIX® RCS graft, made with our CALCIPLEX™ synthetic composite granules, offers a unique bone graft substitute for surgeons wishing to integrate the proven benefits of calcium sulfate activity with a slower resorbing, porous tri-calcium phosphate

scaffold. Launched in early 2005, the product is part of an overall strategy to establish Wright as the global supplier with the broadest offering of bone grafting materials, with both tissue-based DBM (demineralized bone matrix) and completely synthetic options.

Another essential component of our successful biologics line is the GRAFTJACKET® Tissue Membrane family of products. Due to the material's unique ability to quickly remodel into host tissue and restore damaged or diseased tissue to a more normal state, GRAFTJACKET® products have become the "gold standard" for a number of surgical procedures. These products achieved original success in augmentation for bone grafting procedures. However, their use has grown to encompass rotator cuff repair, various ligament and tendon repairs and even treatment of diabetic foot ulcers — a potentially devastating and costly health concern for thousands of patients in the United States alone. Driven by the dramatically successful outcomes of diabetic foot wound patients treated with our GRAFTJACKET® Ulcer Repair Matrix, the Company began an aggressive campaign in late 2004 to obtain crucial Medicare reimbursement codes for this specific use of the product. By January 2005, the Centers for Medicare and Medicaid (CMS) had assigned the codes, thereby providing an avenue of reimbursement for surgeons using our tissue membrane product to treat diabetic foot wounds in a hospital out-patient department, wound care center or the physician's own office. Further penetration of this very large and growing market opportunity is a key priority of the Biologics Marketing Team for 2005.

We are also continuing to receive positive reports concerning use of our new MIIG® X3 HiVisc injectable material in various high strength bone grafting procedures. One such example is osteolysis lesion repair in conjunction with reconstructive hip surgery. Specifically, some surgeons have found the MIIG® X3 HiVisc material useful for filling bony cavities behind and around hip cups and femoral stems, allowing the host tissue to regenerate within the bone voids. The HiVisc material simultaneously adds reinforcement to the surrounding bone and implant as the remodeling of new bone takes place. To assist the surgeon in preparing the bone cavity and removal of the osteolyic lesion, Wright offers a convenient single-use, procedure-specific kit. Some surgeons have also found the MIIG® X3 HiVisc material to be beneficial in certain spine procedures, such as vertebral compression fractures. Surgeons have reported very promising results when using the material in association with Kyphoplasty procedures. While the material is currently cleared for use in instrumented spine procedures, Wright is pursuing approval from the FDA to initiate an IDE (Investigational Device Exemption) clinical study in association with kyphoplasty procedures.

Wright is also continuing to pursue FDA regulatory clearance for its ADCON® Anti-Adhesion Gel technology. Wright's dialogue with the FDA continues on this product and we hope this will lead to regulatory clearance at a future date. This product continues to be marketed and well-received outside of the United States.

In 2004, our small joint extremity business experienced a "new product transitional year," growing at 14% globally due to several key product launch initiatives for the distal radius. Our core finger and toe implant business continues to be a valuable franchise that allows our sales and distribution representatives the ability to readily gain access to hand, trauma and foot surgeons. However, the distal radius anatomy has become one of our key target areas for capturing new customers, expanding use of our biologic grafting products and establishing an additional franchise primarily driven by innovative new products. In 2004, we launched a number of products to support this initiative. First was the LOCON™ VLS Plating System, which combines the benefits of a low-profile stainless steel plate with an anatomic shape for a volar (palm side) surgical approach. The plating system design more closely matches the natural human anatomy, which aids in both placement and bony fragment repositioning during surgery.

Wright also launched the MICRONAIL™ Intramedullary Fracture Fixation System — one of the most exciting products ever introduced for the repair of distal radius fractures. This patented system was developed by Wright in association with the surgeon inventor and has the potential to vastly improve the longer-term outcomes of the common distal radius fracture known as a Colles fracture. Currently, approximately 50% of Colles fractures treated only with a cast at the onset of injury achieve good to excellent results in the long-term. We believe that the MICRONAIL™ System has the potential to significantly improve these long-term outcomes when used in place of common casting procedures. Early clinical evidence supports this belief with the results showing that the MICRONAIL™ implant allows almost immediate early motion, superior anatomic alignment and enhanced bone healing. Clearly, extremities solutions like these represent significant growth potential. Over the course of 2005, we will continue to drive these innovative distal radius products into the market place to create new market opportunities for our Company.

Although the primary supplier of our foot and ankle products announced in 2004 that it would be acquired in an early 2005 transaction, Wright was prepared to continue its participation in the foot and ankle market with a complete and more advanced set of implants and instrumentation known as the CHARLOTTE™ Foot and Ankle system. The new products were introduced into the U.S. market in late February 2005 and will also be integrated into our international distribution network as part of our extremity/small joint product portfolio.

the wright approach to
international results & opportunities

International sales accounted for 39% of Wright's total revenues in 2004, with a year-over-year growth of 22%. We saw some shifting of our growth profile this year, with the contribution of our distributor businesses on a percentage basis growing at higher rates than in past years. Our European business experienced changes in management personnel following the departure of several individuals within our Cremascoli subsidiary. New personnel brought into the business in France, Italy and the United Kingdom all have very solid track records in the orthopaedic medical device field. We are confident that these management changes will result in a stronger European management organization going forward.

In 2004, a great deal of effort and attention was focused on establishing a very close ongoing relationship with Oxford University to facilitate longer-term development projects in both the total hip and total knee arenas. We are quite excited about this new and important relationship, which should provide our European operations a new Center of Excellence for product development and training in future years.

While we were pleased with the performance of our international operations in 2004, our longer-

term goal is to more aggressively develop distribution alliances and partnerships and pursue acquisitions to enhance our presence and complement our more traditional strengths in Europe and Japan.

the wright approach
for the future

Wright's outstanding performance in 2004 could not have been achieved without the ongoing efforts and continuous dedication of our employees worldwide, which were supported by an outstanding Board of Directors and experienced management team. To all who played a role in our success in 2004 — employees, customers and stockholders — we offer our sincere appreciaton and thanks.

As we look ahead to 2005, the market opportunities within our core product areas support a high degree of optimism that Wright will continue to deliver the right product results for patients and financial results for shareholders. But that optimism must be balanced by awareness of the potential for challenges to lie ahead. To both seize the opportunities and successfully face the potential challenges, we have continued to enhance our management team with the addition of a knowledgeable and seasoned President & CEO. Furthermore, our marketing and R&D groups have been restructured to be more closely aligned with the overall product development process, assuring that we have the right products for our customers at the right time. In the coming year, we anticipate continued strong competition in all of our global markets. But with the Wright approach of continued management focus on new products, expanded distribution and shareholder returns, we are ready to deliver another year of the right results.

Sincerely,

F. Barry Bays
Executive Chairman
of the Board of Directors

Laurence Y. Fairey
President, Chief Executive Officer
& Director

the wright results through key international partnerships

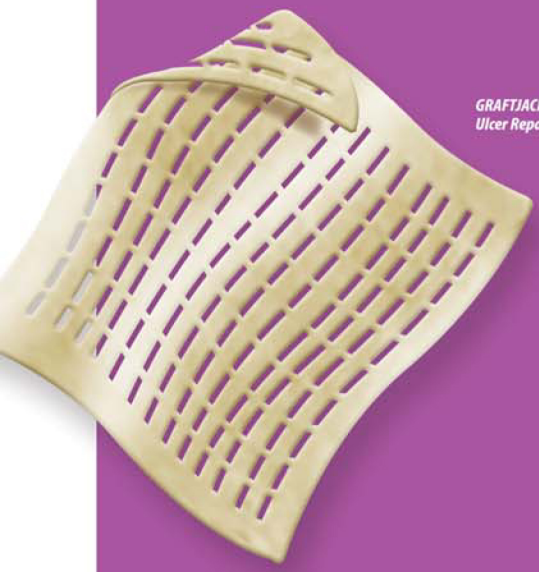
With a growing presence in over 60 countries, international opportunities continue to be a major focus for Wright. In 2004, the Company took an important step in strengthening relationships with its international surgeons through a new partnership with Oxford University.

The collaboration with this world-renowned institution encompasses both development and instructional programs. **The educational component of the partnership focuses on joint resurfacing and is planned to include 3-4 surgeon instructional events at the University each year, establishing a "Center of Excellence" for the international orthopaedic community.**

The first of these programs took place in 2004, hosting over 100 surgeons. Encouraged by the success of the program's initial phase, the Company looks forward to further positive developments through its partnership with Oxford University and hopes to establish similar programs with other prestigious institutions.

Among the oldest and most respected institutions of learning in the world, Oxford University advances research in over 60 disciplines. Academic and research activities in the field of orthopaedics have been conducted at the University since 1937.

the wright approach
to biologic solutions



GRAFTJACKET®
Ulcer Repair Matrix

SOFT TISSUE REPAIR —
GRAFTJACKET® ULCER REPAIR MATRIX

Diabetes is one of the most devastating diseases affecting the United States today, in terms of both patient impact and healthcare costs. About 16 million Americans have been diagnosed with the disease, which not only affects the daily lives and long-term health of patients, but often leads to secondary complications that can have tragic results. One such complication is diabetic foot ulcers.

These challenging wounds affect approximately 15% of Americans with diabetes and are the primary cause of hospital admissions for all diabetics. The wounds are a result of poor lower extremity circulation caused by the disease. Because the reduced circulation is often accompanied by decreased sensation in the affected limbs, many foot ulcers go unnoticed by the patient until they are severe enough to require medical intervention. For many, however, the wounds progress deep into the tissue and severe bacterial infection takes over. **For nearly 70,000 people each year, the result of this scenario has been amputation – until now.**

Through the revolutionary material of GRAFTJACKET® Matrix, Wright is giving even patients with severe foot ulcers the chance for successful treatment without amputation. GRAFTJACKET® Matrix works by allowing healing at deeper levels while protecting the external layer of the wound with a graft material that converts into functional host tissue. In most cases, successful wound repair is achieved following just one treatment with GRAFTJACKET® Matrix, while other available options usually require multiple treatments.

In fact, clinical data currently submitted for publication shows that treatment with the GRAFTJACKET® Matrix is 85% effective at 12 weeks, compared to 5% effectiveness for conventional treatment. With the innovative approach of Wright's GRAFTJACKET® Matrix, physicians and their patients have the benefits of faster, less costly wound repair — the right results for treating diabetic foot ulcers.

photos courtesy of Douglas Stoker, DPM

BONE REPAIR —
IGNITE® INJECTABLE GRAFT

"Being injured is a scary place to be when you are a professional athlete.

I have a family at home that depends on me, and if I hadn't healed 100%, my earning power would certainly have been jeopardized.

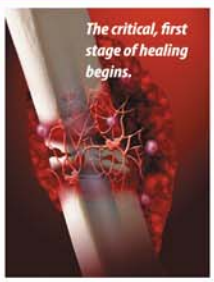
I am so thankful IGNITE® graft worked a miracle and enabled me to continue playing the sport I love at a competitive level."

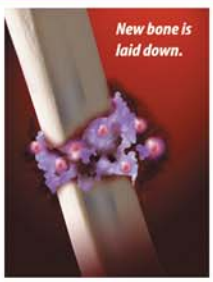
Michael Bennet, professional football player
IGNITE® Injectable Bone Graft Recipient

how does IGNITE® graft heal bone?

IGNITE® graft, an injectable bone-healing stimulant, facilitates the bone healing process by reinforcing and stimulating cellular activity in poorly vascularized areas of bone.

In cases such as Michael's, this minimally-invasive procedure can be performed in an outpatient setting, with results seen as early as 8 weeks.





the wright approach
to extremity solutions

CHARLOTTE™
Foot & Ankle Fixation System

FOOT & ANKLE —
CHARLOTTE™ FIXATION SYSTEM

With so many Americans leading active lifestyles, foot and ankle injuries have become some of the most common conditions treated by orthopaedic specialists. Sprains, strains, stress fractures and more severe foot and ankle injuries send millions in search of medical care each year. In addition, the extreme forces exerted on the foot and ankle through even simple daily activities make the area especially susceptible to chronic injury and pain. For some patients, the solution is reconstructive fixation of the affected bones through use of an implant.

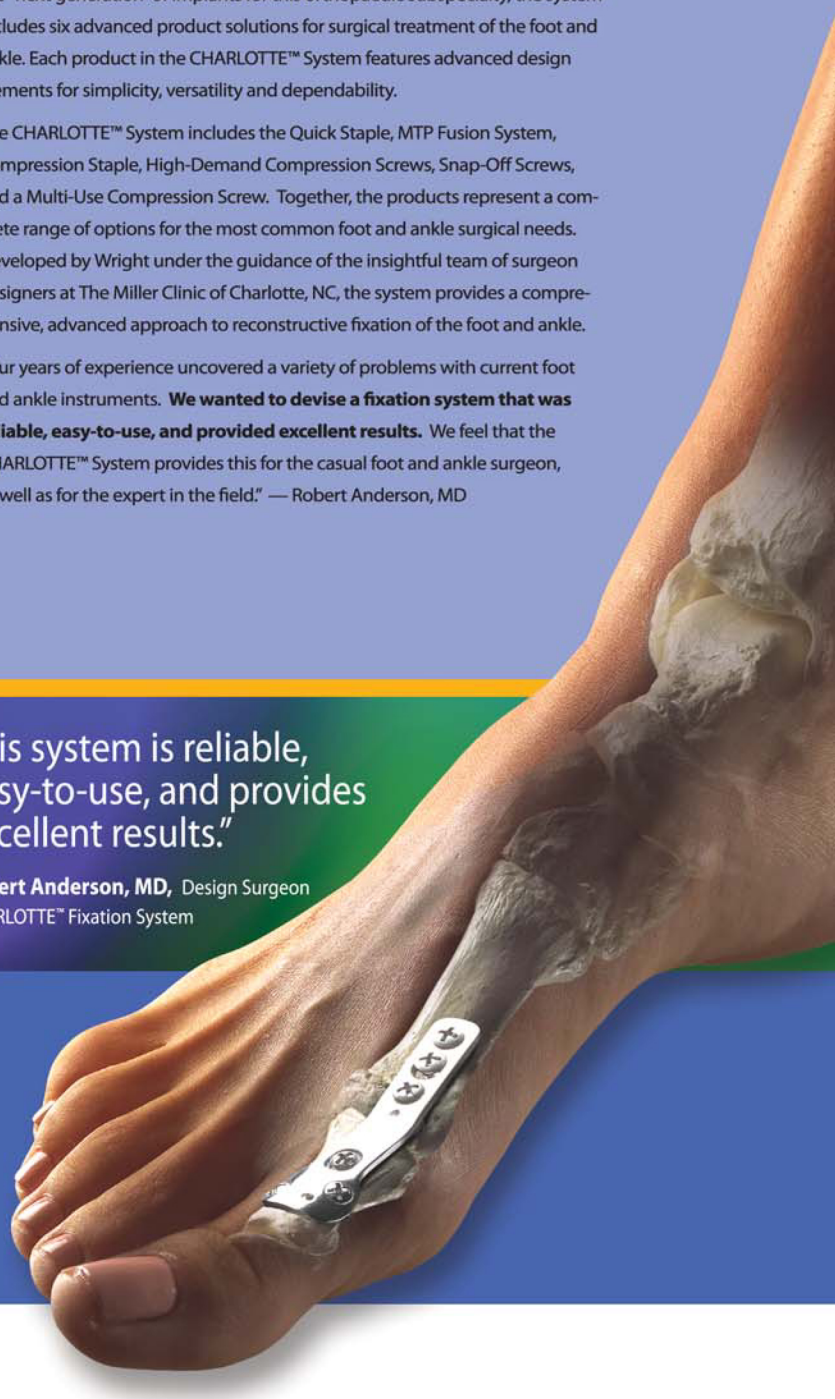
When fixation is required, successful treatment demands a device that suits the special needs of this complex set of small bones. To meet these needs, Wright offers the CHARLOTTE™ Foot & Ankle Fixation System. Designed as the "next generation" of implants for this orthopaedic subspecialty, the system includes six advanced product solutions for surgical treatment of the foot and ankle. Each product in the CHARLOTTE™ System features advanced design elements for simplicity, versatility and dependability.

The CHARLOTTE™ System includes the Quick Staple, MTP Fusion System, Compression Staple, High-Demand Compression Screws, Snap-Off Screws, and a Multi-Use Compression Screw. Together, the products represent a complete range of options for the most common foot and ankle surgical needs. Developed by Wright under the guidance of the insightful team of surgeon designers at The Miller Clinic of Charlotte, NC, the system provides a comprehensive, advanced approach to reconstructive fixation of the foot and ankle.

"Our years of experience uncovered a variety of problems with current foot and ankle instruments. **We wanted to devise a fixation system that was reliable, easy-to-use, and provided excellent results.** We feel that the CHARLOTTE™ System provides this for the casual foot and ankle surgeon, as well as for the expert in the field." — Robert Anderson, MD

"This system is reliable, easy-to-use, and provides excellent results."

Robert Anderson, MD, Design Surgeon
CHARLOTTE™ Fixation System



HAND & WRIST —
MICRONAIL™ DISTAL RADIUS SYSTEM

"The first time I broke my wrist, it was excrutiatingly painful for a month.

The second time I broke it ... when I saw the x-ray ... I thought my wrist would never be put back together again.

But, it was fixed & it's almost perfect. It actually doesn't hurt at all.

Thank goodness for this 'magic nail'."

Francis Edwards, 63-year-old
MICRONAIL™ Distal Radius System Recipient

why is the MICRONAIL™ system a better solution?

300,000 fractures of the wrist are treated in the US each year.

Traditional treatment options can have complications, including pain and loss of function caused by an implant placed on the exterior of the bone. The MICRONAIL™ system addresses these common concerns and also allows patients limited use of their injured wrist almost immediately following surgery.

The MICRONAIL™ system is implanted, uniquely, inside the bone, providing immediate stabilization and eliminating the possibility of irritation to surrounding soft tissue. In addition, the less invasive approach used to implant the device allows patients a more speedy recovery.

Traditional plating systems typically require a 5-6 inch incision. Conversely, the MICRONAIL™ system requires only a 2-3cm incision – thereby, allowing for a minimally-invasive approach to surgery.

Also contrary to traditional plating systems, the MICRONAIL™ device is housed completely within the bone, not on top ... eliminating painful friction between implant and skin.

Flexibility is restored.

the wright approach
to hip solutions

ADVANCED BEARING SURFACES — CERAMIC-ON-CERAMIC

For decades, hip implants were designed to meet the needs of the most common patient profile: older and less active. For these patients, an artificial joint comprised of metal and a plastic called polyethelene achieved good results, although the materials would wear over time, usually leading to revision surgery. But a growing segment of today's patient population has a younger face with more demanding needs. **For years, younger patients suffering from chronic hip pain were simply advised to treat the discomfort, avoid some activities they enjoyed, and postpone surgery for as long as possible because traditional implant materials could not provide long-term performance for their higher activity levels.** But now those patients have options.

For younger, more active patients, Wright offers advanced bearing options, such as the LINEAGE® Ceramic-On-Ceramic Acetabular System. The system replaces the traditional material combination of metal on plastic with two alumina oxide ceramic components for greater strength and significantly reduced wear. The result is an implant that can withstand the tremendous forces of an active lifestyle – and restore confidence, freedom and pain-free mobility to people facing debilitating hip disease at an early age. Through the advanced bearing options of the LINEAGE® Acetabular System, Wright is helping a growing number of younger patients achieve the right results for their active lives.

LINEAGE® Ceramic Hip

"It's amazing. I can do everything without pain. I'm a whole person."

Peggy Nicolai, 49-year-old
LINEAGE® Ceramic Hip Recipient

When she was just a small baby, physicians did not think Virginia Atkins, now 26 and a mother of two, would ever be able to walk. Doctors attempted to fix a deformity of her hip socket through surgery and Virginia did go on to develop normally.

However, as she grew older, she experienced hip pain that became significantly worse. Routine activities like getting out of bed and shopping were becoming more and more painful.

She sought the advice of Dr. John Mays, an orthopaedic surgeon in Shreveport, LA. Due in no small part to her young age, Dr. Mays recommended Wright's ceramic hip as a treatment option.

Virginia had hip replacement surgery in May 2004 and has seen significant improvements in her pain level and mobility. She no longer dreads facing everyday tasks like walking up stairs, and is glad she made the right decision to treat her condition.

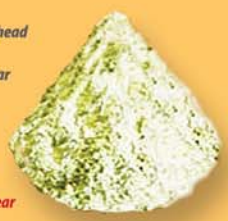
"WEARS" the proof?

Friction that is caused by the rubbing together of the acetabulum (hip socket) and femoral head components of a total hip replacement eventually leads to these implant parts wearing. Ceramic components have demonstrated superior wear characteristics in clinical trials / wear simulation testing.

Ceramic-Ceramic components wear rate is only:
0.002mm / year

Ceramic-Plastic components wear rate is:
0.05-0.1mm / year

Metal-Plastic components wear rate is:
0.1-0.4mm / year



the wright approach to knee solutions

MIS TECHNIQUES — ADVANCE® KNEE SYSTEM

Minimally-invasive surgery (MIS) options are among the most revolutionary advances in orthopaedics. Both patients and surgeons can appreciate the advantages of a smaller incision, including reduced recovery time and costs. For the more than 350,000 Americans facing total knee replacement surgery each year, these are especially attractive benefits. To help surgeons provide these benefits to their patients, Wright developed a less invasive surgical approach for use with its ADVANCE® series of knee products – an innovative implant line designed to provide patients with more natural knee movement. The approach combines a specially designed instrument system and refined surgical technique to help surgeons perform less invasive total knee procedures without a radical shift from their familiar techniques.

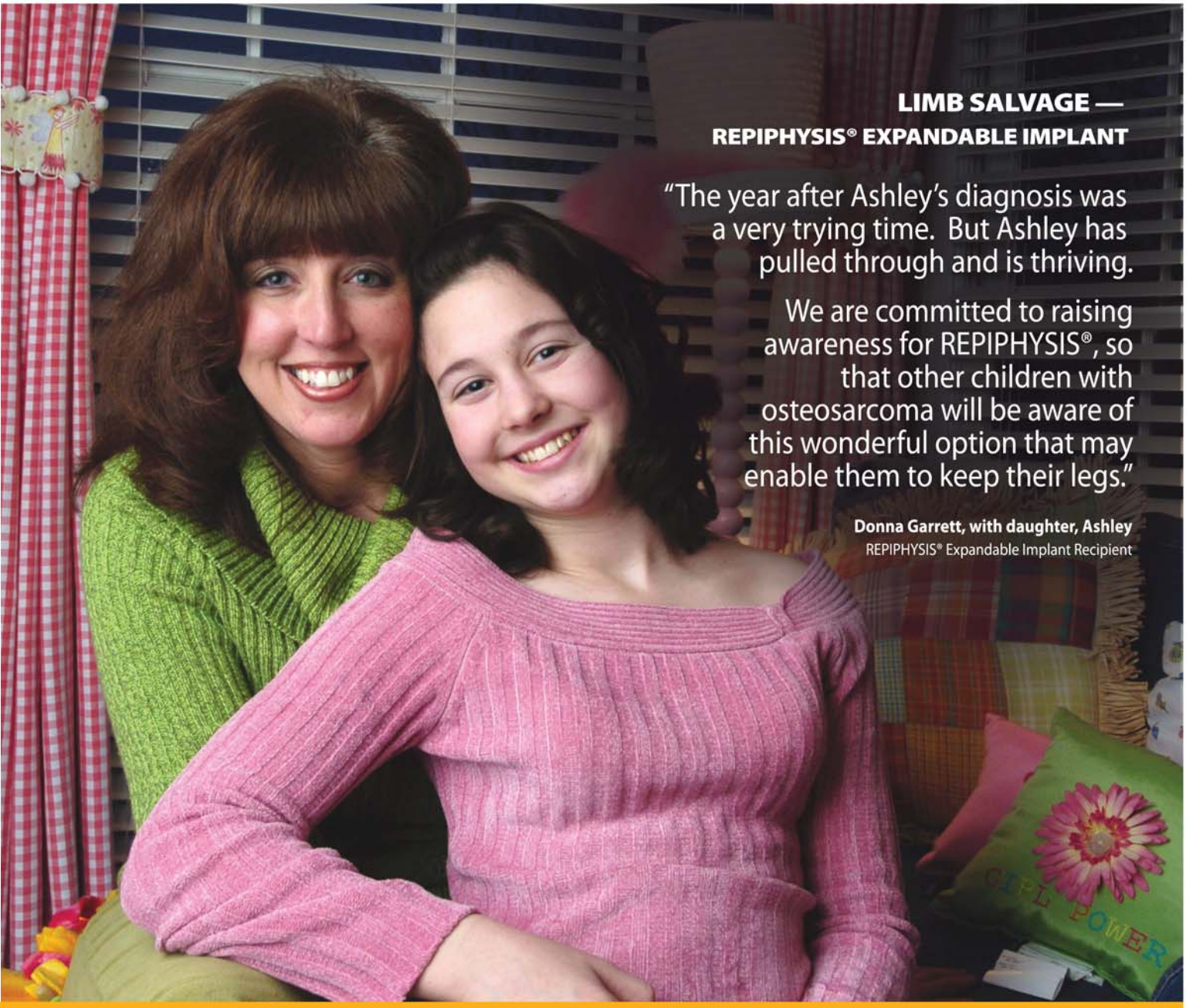
With Wright's instrumentation and simplified MIS technique, patients get back on their feet more quickly following surgery — and they move on to experiencing the benefits of their "new knee." In most cases, it also leaves a significantly smaller surgical scar.

These results are part of Wright's ODYSSEY™ Tissue Preserving Initiative, a minimally invasive surgery program for hip and knee procedures. Through simplified surgical techniques, advanced instrumentation, and innovative implant options, the ODYSSEY™ program is helping surgeons and their patients achieve MIS success.

ADVANCE® Medial-Pivot Knee

"After getting my new knees, I can go distances without pain."

Maggie Bala, 60-year-old ADVANCE® Knee Recipient



LIMB SALVAGE — REPIPHYSIS® EXPANDABLE IMPLANT

"The year after Ashley's diagnosis was a very trying time. But Ashley has pulled through and is thriving.

We are committed to raising awareness for REPIPHYSIS®, so that other children with osteosarcoma will be aware of this wonderful option that may enable them to keep their legs."

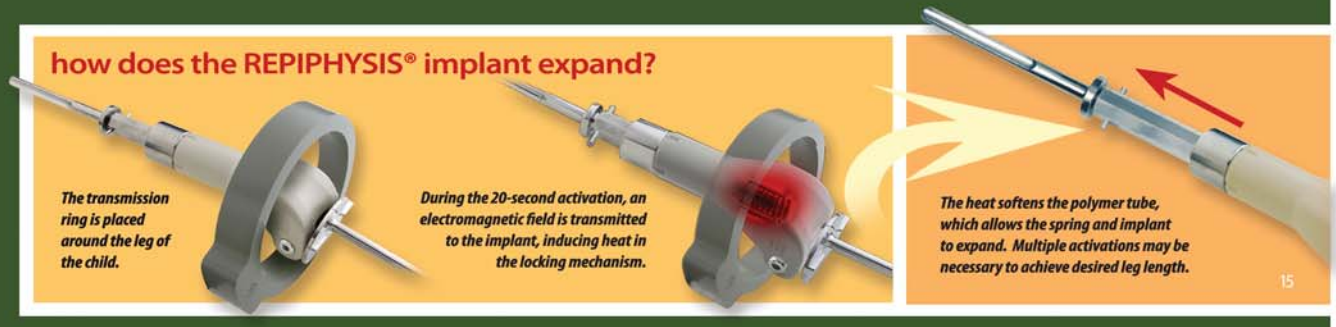
Donna Garrett, with daughter, Ashley
REPIPHYSIS® Expandable Implant Recipient

In 2002, Ashley Garrett was diagnosed with osteosarcoma, the most common type of bone cancer in children. After four rounds of chemotherapy, the size of her tumor was successfully reduced and could be removed surgically. However, because of its location, Ashley's growth plate would also have to be removed.

As a replacement for the bone to be removed, Dr. Michael Neel of St. Jude Children's Research Hospital in Memphis, TN, suggested the REPIPHYSIS® Expandable Implant. The REPIPHYSIS® Implant is the first bone replacement that does not require additional surgeries to lengthen the implant as a child's healthy limb grows.

The Garretts were thrilled that their daughter would not need an amputation and would be able to keep her leg. The surgery was a success and now, more than two years later, Ashley is functioning and thriving as a normal twelve-year-old.

how does the REPIPHYSIS® implant expand?



The transmission ring is placed around the leg of the child.

During the 20-second activation, an electromagnetic field is transmitted to the implant, inducing heat in the locking mechanism.

The heat softens the polymer tube, which allows the spring and implant to expand. Multiple activations may be necessary to achieve desired leg length.

senior management & directors

senior management

Laurence Y. Fairey
President, CEO & Director

John K. Bakewell
EVP & Chief Financial Officer

R. Glen Coleman
President, US Sales & Marketing

Brian T. Ennis
President, International

Jeffrey G. Roberts
SVP & Chief Technology Officer

William S. Flannery
VP, Logistics & Materials

Kyle M. Joines
VP, Manufacturing

Jason P. Hood
VP, General Counsel & Secretary

Lance A. Berry
VP & Corporate Controller

Aldo M. Denti
VP & GM, Ortho Recon

Karen L. Harris
VP, International Sales & Distribution

Joyce B. Jones
VP & Treasurer

Steven A. Kahn
VP, Regulatory Affairs & Quality Systems

William F. Scott
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Michael B. Sheldon
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Joseph J. Sinkovich
VP, US Sales

John T. Treace
VP & GM, Biologics & Extremities

Stephen E. White
VP, Development – Ortho Recon

directors

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Executive Chairman of the Board
Wright Medical Group, Inc.
Director since 2000.

Laurence Y. Fairey
President & Chief Executive Officer
Wright Medical Group, Inc.
Director since 2004.

Richard B. Emmitt
Managing Director,
The Vertical Group, Inc.
Director since 1999.

David D. Stevens
Chairman of the Board & CEO
Accredo Health, Inc.
Director since 2004.

James E. Thomas
Managing Partner
Thomas, McNerney & Partners, LLC
Director since 2000.

Thomas E. Timbie
President, Timbie and Company, LLC
Chief Financial Officer, ev3, Inc.
Director since 2000.

James T. Treace
President
The J & A Group, LLC
Director since 1999.

Elizabeth H. Weatherman
Managing Director
Warburg Pincus, LLC
Director since 1999.

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Elizabeth H. Weatherman

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Richard B. Emmitt
James E. Thomas
Thomas E. Timbie

Compensation Committee
David D. Stevens
James E. Thomas
Elizabeth H. Weatherman

Nominating & Corporate Governance Committee
Richard B. Emmitt
Thomas E. Timbie
Elizabeth H. Weatherman

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Executive Overview

Company Description. We are a global orthopaedic medical device company specializing in the design, manufacture and marketing of reconstructive joint devices and biologics products. Reconstructive joint devices are used to replace knee, hip and other joints that have deteriorated through disease or injury. Biologics are used to replace damaged or diseased bone, to stimulate bone growth, and to provide other biological solutions for surgeons and their patients. We have been in business for over 50 years and have built a well-known and respected brand name and strong relationships with orthopaedic surgeons.

Our corporate headquarters and U.S. operations are located in Arlington, Tennessee, where we conduct our domestic research and development, manufacturing, warehousing, and administrative activities. Outside the U.S., we have research and development, manufacturing, and administrative facilities in Toulon, France; research, distribution and administrative facilities in Milan, Italy; and sales and distribution offices in Canada, Japan and Europe. We market our products in over 60 countries through a global distribution system that consists of a sales force of approximately 700 individuals who promote our products to orthopaedic surgeons and hospitals. At the end of 2004, we have 318 exclusive independent distributors and sales associates in the U.S., and approximately 400 sales representatives internationally who are employed through a combination of our stocking distribution partners and direct sales offices.

Company History. We were incorporated in November 1999 as a Delaware corporation, and had no operations until December 7, 1999, when we were reorganized by an investment group through the acquisition of our predecessor company, Wright Medical Technology, Inc. This transaction represented a recapitalization of our predecessor company and the inception of Wright in its present form. On December 22, 1999, we acquired Cremascoli Ortho Holding, S.A., an orthopaedic medical device company headquartered in Toulon, France. In 2001, we completed our IPO of 7,500,000 shares of common stock, which generated $84.8 million in net proceeds. In 2002, we completed a secondary offering of 3,450,000 shares of common stock which generated $49.5 million in net proceeds.

Principal Products. We primarily sell reconstructive joint devices and biologics products. Our reconstructive joint device sales are derived from three primary product lines: knees, hips and extremities. Our biologics sales encompass a broad portfolio of products designed to stimulate and augment the natural regenerative capabilities of the human body. We also sell various orthopaedic products not considered to be part of our knee, hip, extremity or biologics product lines.

Our hip joint reconstruction product portfolio provides offerings in the areas of bone-conserving implants, total hip reconstruction, revision replacement implants, and limb preservation. Our hip joint products include the CONSERVE® family of products, the PROFEMUR® Hip System, the LINEAGE® Acetabular System, the ANCA-FIT™ Hip System, and the PERFECTA® Hip System. In 2003, the FDA granted us approval to market our ceramic-on-ceramic bearing as part of the LINEAGE® Acetabular System, placing us among the first companies to market ceramic-on-ceramic total hip solutions in the U.S.

Our biologics products focus on biological musculoskeletal repair and include synthetic and human tissue-based materials. Our principal biologics products include the ALLOMATRIX® line of injectable tissue-based bone graft substitutes, the GRAFTJACKET® tissue repair and containment membranes, the OSTEOSET® synthetic bone graft substitute, the MIIG® family of minimally invasive injectable synthetic bone grafts, and in our international markets, the ADCON® Gel anti-adhesion product.

We offer extremity products for the hand, wrist, elbow, shoulder, foot and ankle in a number of markets worldwide. Our principal extremity products include the Swanson line of finger and toe joint replacement products, the ORTHOSPHERE® Carpometacarpal Implant for repair of the basal thumb joint, the EVOLVE® Modular Radial Head device, the LOCON-T® Distal Radius Plating System, the MICRONAIL™ intramedullary wrist fracture repair system, and the CHARLOTTE™ Foot and Ankle System, a line of comprehensive foot and ankle implants.

Our knee reconstruction products position us well in the areas of total knee reconstruction, revision replacement implants, and limb preservation products. Our principal knee products include the ADVANCE® Knee System and the ADVANCE® Unicompartmental Knee System.

Significant Business Developments. The significant growth of our business that we experienced in 2003 continued into 2004, with considerable expansion of all of our principal product line sales. Net sales grew 20% in 2004, totaling $297.5 million, compared to $248.9 million in 2003. Our focus on the high growth sectors of the orthopaedic industry, such as advanced bearing surfaces, modular necks and bone conserving implants within the hip market and the integration of biologics products into reconstructive joint procedures and other orthopaedic applications, combined with new product development focused on specific surgical issues, continues to drive our success. Our hip and biologics product lines contributed significantly to our performance in 2004, achieving 27% and 24% growth rates, respectively.

A significant development in the hip market over the past two years has been advances in bearing surfaces, including ceramic-on-ceramic. In 2003, the FDA granted us approval to market our ceramic-on-ceramic bearing as part of the LINEAGE® Acetabular System, placing us among the first companies to market ceramic-on-ceramic total hip solutions in the U.S. While we encountered additional competition in the ceramic-on-ceramic hip market in 2004, we sustained a considerable growth rate throughout the year, ending 2004 with an overall growth rate of 27%. We anticipate further competition in the ceramic-on-ceramic hip market in 2005; however, we believe that our full continuum of hip products will position us for continued success in 2005.

In March 2004, our PMA application for our CONSERVE® Plus Hip System was accepted for filing by the FDA. Our CONSERVE® Plus Resurfacing Implant is available outside the U.S. and is pending FDA clearance for the U.S. market. With our CONSERVE® Plus Resurfacing Implant, the surface of the patient's femoral head and the acetabular surface are replaced with minimal bone loss. In May 2004, we received a warning letter from the FDA regarding the CONSERVE® Plus Resurfacing Implant investigational device exemption. We responded in June 2004, addressing the issues cited in the warning letter, and in reply, the FDA informed us that our corrective actions had been accepted. We continue to work with the FDA as it reviews this PMA.

In March 2004, we received marketing clearance from the FDA for our ALLOMATRIX® Injectable Putty. This clearance was obtained based on satisfaction of the FDA's requirements pursuant to a 510(k) premarket notification process that began with our submission of a 510(k) in March

2002. This submission was in response to the FDA's clarification to all allograft putty providers, including us, that such products should be regulated under the medical device premarket notification provisions of the Food, Drug, and Cosmetic Act. Further, in July 2004, we received marketing clearance from the FDA for our ALLOMATRIX® C, ALLOMATRIX® Custom and ALLOMATRIX® DR putty products following our submission of a 510(k) in April 2004, completing the clearance process for our entire ALLOMATIX® family of products.

In August 2004, we introduced our MICRONAIL™ intramedullary wrist fracture repair system, a next-generation, minimally invasive solution that provides immediate fracture stabilization utilizing fixed-angle locking screws. The MICRONAIL™ system is targeted to become a viable alternative for many wrist fracture patients currently treated with a cast and is the only one of its kind on the market.

In September 2004, we announced a voluntary market withdrawal of a limited number of metal acetabular hip cups intended for use in our CONSERVE® hip systems, as these components may not have met our product specifications due to the presence of a small ridge on the cup's non-articulating inside bearing surface. We notified the FDA of this action and removed from commercial availability all unused components covered by the market withdrawal. In connection with this market withdrawal, we incurred approximately $800,000 of expenses for probable costs related to the market withdrawal. We did not experience any supply issues as a result of this market withdrawal, and this market withdrawal has not had a significant impact on our sales. Further discussion of our voluntary market withdrawal is included in Note 15 to our consolidated financial statements in this report.

During the fourth quarter of 2004, we incurred approximately $2.9 million of costs as a result of the transition from certain of our foot and ankle implant offerings to an innovative, next-generation line of internally developed products, collectively referred to as the CHARLOTTE™ Foot and Ankle System, replacing products supplied by a third party vendor pursuant to a distribution agreement that expired in the first quarter of 2005. These charges resulted from the write down of our distributed foot and ankle implant inventory to its estimated net realizable value and accelerated depreciation on the related surgical instrumentation. We launched our CHARLOTTE™ Foot and Ankle System in mid-February 2005.

Significant Industry Factors. Our industry is impacted by numerous competitive, regulatory and other significant factors. The growth of our business relies on our ability to continue to develop new products and innovative technologies, obtain regulatory clearance and compliance for our products, protect the proprietary technology of our products and our manufacturing processes, manufacture our products cost-effectively, respond to competitive pressures specific to each of our geographic markets, including our ability to enforce non-compete agreements, and successfully market and distribute our products in a profitable manner. We, and the entire industry, are subject to extensive governmental regulation, primarily by the FDA. Failure to comply with regulatory requirements could have a material adverse effect on our business. Additionally, our industry is highly competitive and our success is dependent on our ability to compete successfully against our competitors. We devote significant resources to assessing and analyzing competitive, regulatory and economic risks and opportunities. A detailed discussion of these and other factors is provided under the heading, "Factors Affecting Future Operating Results," within MD&A.

Net Sales and Expense Components

Net sales. We derive our net sales primarily from the sale of reconstructive joint devices and biologics products. An overview of our principal product lines is provided under the heading, "Executive Overview," within MD&A.

Cost of sales. Our cost of sales consists primarily of direct labor, allocated manufacturing overhead, raw materials and components, charges incurred for excess and obsolete inventories, royalty expenses associated with licensing technologies used in our products or processes, and certain other period expenses.

Selling, general and administrative. Our selling, general and administrative expenses consist primarily of salaries, sales commissions, royalty and consulting expenses associated with our medical advisors, marketing costs, facility costs, legal costs, other general business and administrative expenses, and depreciation expense associated with surgical instruments required by surgeons to use when implanting our products.

Research and development. Research and development expense includes costs associated with the design, development, testing, deployment, enhancement and regulatory approval of our products.

Amortization of intangible assets. Our intangible assets consist of purchased intangibles principally related to completed technology, distribution channels and trademarks primarily resulting from our 1999 acquisition of Cremascoli, as well as distribution and product licenses. We amortize intangible assets over periods ranging from 1 to 15 years.

Stock-based expense. We incur stock-based expenses as a result of the amortization of non-cash deferred compensation that is recorded in accordance with Accounting Principles Board (APB) Opinion No. 25. This deferred compensation resulted following the issuance of stock options to employees and the sale of equity securities when the estimated fair value of the securities was deemed, for financial reporting purposes, to have exceeded their respective exercise or sales price. The substantial majority of our stock-based expense relates to the issuance of shares and options prior to the completion of our IPO in 2001. Additionally, for stock-based incentives granted to consultants, we defer and amortize the fair value of such grants as calculated pursuant to Statement of Financial Accounting Standards (SFAS) No. 123. Deferred compensation is amortized on a straight-line basis over the respective vesting periods of the stock-based incentives, which is generally four years, and we immediately expense all stock-based compensation associated with the issuance of equity where no vesting restrictions apply.

Interest expense, net. Interest expense, net, consists primarily of interest on borrowings outstanding under our senior credit facility and certain of our factoring agreements, as well as non-cash expenses associated with the amortization of deferred financing costs resulting from the origination of our senior credit facility. These expenses are offset by income earned on our invested cash balances.

Provision for income taxes. We record provisions for income taxes on earnings generated by both our domestic and international operations. Historically, our effective tax rates have varied from our statutory tax rates primarily due to research and development credits and changes in estimates related to our valuation allowances recorded against our net deferred tax assets.

Results of Operations

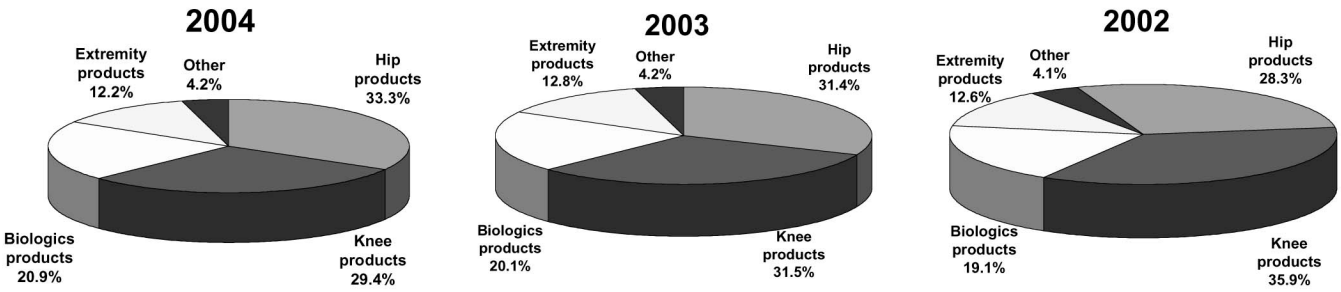
Introduction. The following table sets forth, for the periods indicated, our results of operations expressed as dollar amounts (in thousands) and as percentages of net sales:

Year Ended December 31,	2004		2003		2002	
	Amount	% of Sales	Amount	% of Sales	Amount	% of Sales
Net sales	$297,539	100.0 %	$248,932	100.0 %	$200,873	100.0 %
Cost of sales	84,183	28.3 %	67,815	27.2 %	55,616	27.7 %
Gross profit	213,356	71.7 %	181,117	72.8 %	145,257	72.3 %
Operating expenses:						
Selling, general and administrative	151,144	50.8 %	127,612	51.3 %	106,875	53.2 %
Research and development	18,421	6.2 %	16,151	6.5 %	10,357	5.2 %
Amortization of intangible assets	3,889	1.3 %	3,562	1.4 %	3,946	2.0 %
Stock-based expense	1,489	0.5 %	2,068	0.8 %	1,724	0.8 %
Acquired in-process research and development costs	-	-	4,558	1.8 %	-	-
Arbitration settlement award	-	-	-	-	(4,200)	(2.1)%
Total operating expenses	174,943	58.8 %	153,951	61.8 %	118,702	59.1 %
Operating income	38,413	12.9 %	27,166	10.9 %	26,555	13.2 %
Interest expense, net	1,064	0.4 %	1,107	0.4 %	938	0.5 %
Other income, net	(74)	0.0 %	(1,060)	(0.4)%	(1,277)	(0.6)%
Income before income taxes	37,423	12.6 %	27,119	10.9 %	26,894	13.4 %
Provision for income taxes	13,401	4.5 %	9,722	3.9 %	1,834	0.9 %
Net income	$24,022	8.1 %	$17,397	7.0 %	$25,060	12.5 %

The following table sets forth our net sales by product line for the periods indicated (in thousands), and the percentage of year-over-year change:

	Year Ended December 31, 2004	Year Ended December 31, 2003	2004 vs. 2003 % Change	Year Ended December 31, 2003	2003 vs. 2002 % Change
Hip products	$99,133	$78,071	27.0%	$56,945	37.1%
Knee products	87,408	78,338	11.6%	72,058	8.7%
Biologics products	62,070	50,056	24.0%	38,347	30.5%
Extremity products	36,433	31,876	14.3%	25,367	25.7%
Other	12,495	10,591	18.0%	8,156	29.9%
Total net sales	$297,539	$248,932	19.5%	$200,873	23.9%

The following graphs illustrate our product line sales as a percentage of total net sales for the years ended December 31, 2004, 2003, and 2002:



Comparison of the year ended December 31, 2004 to the year ended December 31, 2003

Net sales. Net sales growth in 2004 was attributable to strong demand across all of our principal products lines, with significant contributions from hips and biologics which grew by 27% and 24%, respectively, and solid growth in our extremity and knee business which grew by 14% and 12%, respectively. Geographically, our domestic net sales totaled $180.4 million in 2004 and $152.9 million in 2003, representing approximately 61% of total net sales in both years and growth of 18%. Our international net sales totaled $117.2 million in 2004, a 22% increase as compared to net sales of $96.1 million in 2003. Our 2004 international net sales include a favorable currency impact of approximately $8.1 million, principally resulting from the 2004 performance of the euro against the U.S. dollar. Our international growth was primarily driven by increased sales in our European and Asian markets, with expansion across all product lines.

Our hip product sales totaled $99.1 million in 2004, representing a 27% increase. Growth in our hip business in 2004 is attributable to continued success in domestic markets, where total hip procedures grew by 20%, driven by our CONSERVE® Total Implant with BFH™ Technology and our PROFEMUR® line of primary stems featuring our innovative neck modularity. Additionally, a favorable shift in our sales mix to premium priced hard bearing procedures, which includes our ceramic-on-ceramic and metal-on-metal products, contributed to our domestic growth. Our percentage of hard bearing surgeries grew from 57% of total domestic hip surgeries in 2003 to 66% in 2004. In our international markets, unit sales growth of our CONSERVE® Plus Resurfacing Implant and a favorable currency impact of $4 million both impacted the year over year sales increase. We believe that our hip product portfolio, which focuses on innovative solutions including bone-conserving implants, advanced bearing surfaces and modular neck technology, will position us for continued success in 2005.

Sales of our biologics products in 2004 totaled $62.1 million, representing an increase of 24%. The growth of our biologics business in 2004 is primarily attributable to the continued favorable performance, in domestic markets, of our GRAFTJACKET® tissue repair and containment membranes combined with the performance of our ADCON® Gel product in international markets. Domestically, total biologics procedures grew by 4%, as significant growth of our GRAFTJACKET® product line, combined with growth of our OSTEOSET® family of products and our MIIG® (Minimally Invasive Injectable Graft) family of products, was offset by declines in our DBM (demineralized bone matrix) containing ALLOMATRIX® family of products. During 2004, competitive pressures in the mature market for DBM containing products had a negative impact on the performance of our ALLOMATRIX® products. From an international perspective, unit sales growth of our ADCON® Gel product and a favorable currency impact of approximately $400,000 contributed to our biologics growth in 2004. As we move into 2005, significant investment in high performance synthetic bone graft substitutes should enable us to take advantage of longer-term opportunities within the trauma and spine segments of the orthopaedic market.

Our extremity product sales increased to $36.4 million in 2004, representing growth of 14% over 2003. Increased unit sales of our higher priced extremity products, such as our foot and ankle products and our EVOLVE® Modular Radial Head System, combined with pricing increases across our entire extremity product platform, were the most significant factors contributing to our year over year growth. For 2005, we anticipate that our extremity line of business will continue to benefit from our EVOLVE® Modular Radial Head System, as well as the 2004 launch of our MICRONAIL™ system and our mid-February 2005 launch of our CHARLOTTE™ Foot and Ankle System, a next-generation line of internally developed foot and ankle products.

Sales of our knee products totaled $87.4 million in 2004, representing growth of 12%. Our domestic knee performance is attributable to a combination of increased unit sales and increased prices. Our international knee growth is attributable to a combination of increased unit sales and a favorable currency impact of approximately $2.4 million. In the latter half of 2004, we introduced our minimally invasive surgical instrumentation for knee procedures to certain key customers. As we move into 2005, we anticipate further success in our knee product line as we are able to more fully penetrate the U.S. market with this instrumentation.

Cost of sales. Cost of sales as a percentage of net sales increased to 28.3% in

2004 from 27.2% in 2003. Approximately 0.8 percentage points of this increase is attributable to $2.4 million of costs incurred during the fourth quarter of 2004 to write down certain foot and ankle implant inventory to its net realizable value as a result of the transition of this product line to our CHARLOTTE™ Foot and Ankle System. The remaining increase as a percentage of sales is primarily attributable to higher levels of charges incurred for excess and obsolete inventories. Our cost of sales and corresponding gross profit percentages can be expected to fluctuate in future periods depending upon changes in our product sales mix and prices, distribution channels and geographies, manufacturing yields, period expenses and levels of production volume.

Selling, general and administrative. Our selling, general and administrative expenses as a percentage of net sales totaled 50.8% in 2004, a 0.5 percentage point decrease from 51.3% in 2003. This decrease is attributable to decreased royalty expenses as a percentage of net sales, decreased commission expense as a percentage of net sales due to shifts in our geographic sales mix to higher levels of international sales which generally incur a lower commission rate, and our ability to control other discretionary costs while continuing to significantly expand our business. These decreases were offset by approximately $1.2 million of incremental costs related to corporate governance, approximately $700,000 resulting from our limited market withdrawal of certain CONSERVE® hip components, approximately $500,000 of accelerated depreciation expense related to surgical instrumentation for certain foot and ankle products that will be transitioned out of our product offerings during the first quarter of 2005, and additional legal costs related to the on-going transition of certain management and distribution personnel in Southern Europe.

We anticipate that our selling, general and administrative expenses as a percentage of net sales will continue to decrease in future periods as we manage the growth of our existing infrastructure while continuing to expand our business. During the first half of 2005, we expect our selling, general and administrative expenses to be impacted by additional costs associated with the transition of certain management and distribution personnel in Southern Europe and additional accelerated depreciation on surgical instrumentation. Additionally, selling, general and administrative expenses will increase in absolute dollars to the extent that any additional growth in net sales results in increases in sales commissions and royalty expense associated with those sales.

Research and development. Our investment in research and development activities represented approximately 6.2% of net sales in 2004, as compared to 6.5% in 2003. In absolute dollars, research and development expenditures increased to $18.4 million in 2004 from $16.2 million in 2003. This increase can be attributed to increased spending on product development and clinical evaluations for pre-market products and products already on the market. Our key product launches in 2004 included our OSTEOSET® DBM Pellets, our ADVANCE® Double-High Knee design, our MICRONAIL™ intramedullary distal radius implant, our ODYSSEY™ Tissue Preserving Initiative for Hip and Knee procedures, and our PROFEMUR® Tapered Stem Total Hip System.

For 2005, we anticipate that our research and development expenditures as a percentage of net sales will be in the range of 6% to 7%. As our business continues to grow, we expect our research and development expenditures to increase in absolute dollars, and may increase as a percentage of net sales as we continue to increase our investment in product development initiatives and clinical studies.

Amortization of intangible assets. Our amortization expense during 2004 was consistent with 2003, totaling $3.9 million in 2004 as compared to $3.6 million in 2003. Based on the intangible assets held at December 31, 2004, we expect to amortize approximately $4.0 million in 2005, $3.5 million in 2006, $2.9 million in 2007, $2.7 million in 2008 and $2.5 million in 2009.

Stock-based expense. We recognized $1.5 million and $2.1 million of stock-based expense during 2004 and 2003, respectively, primarily resulting from the amortization of our deferred compensation. In December 2004, the Financial Accounting Standards Board (FASB) issued SFAS No. 123 (Revised 2004), "Share Based Payment" (SFAS No. 123R), which requires the recognition of compensation expense for the fair value of share-based transactions. The fair value must be determined as of the date of grant using a valuation model such as Black-Scholes or a lattice model. The resulting compensation expense will be recognized over the service period. We will adopt SFAS No. 123R effective July 1, 2005. We anticipate that we will record material amounts of incremental non-cash stock-based expense in future periods following the adoption of SFAS No. 123R. However, the exact amount cannot be determined until management's evaluation of SFAS No. 123R is complete and an appropriate valuation model has been selected and applied to determine the fair value of our stock options outstanding. The effect of expensing stock options on our historical results of operations using the Black-Scholes model is presented in the table in Note 2 to our consolidated financial statements in Item 8 of this report.

In-process research and development cost. Upon consummation of our acquisition of certain ADCON® Gel technology assets from Gliatech Inc. in March 2003, we immediately recognized as expense approximately $4.6 million in costs representing the estimated fair value of acquired in-process research and development (IPRD) that had not yet reached technological feasibility and had no alternative future use (see Note 3 to our consolidated financial statements in this report).

We engaged an independent third party to conduct a valuation of the intangible assets acquired. The value was determined by estimating the costs to develop the acquired IPRD into commercially viable products, estimating the resulting net cash flows from this project, and discounting the net cash flows back to their present values. An additional discount was applied to take into account the uncertainty surrounding the successful development and commercialization of the acquired IPRD. The resulting net cash flows from the project were based on our management's best estimates of revenue, cost of sales, research and development costs, selling, general and administrative costs, and income taxes from the project. A summary of the estimates used to calculate the net cash flows for the project is as follows:

Project	Year net cash in-flows expected to begin	Discount rate including factor to account for uncertainty of success	Acquired IPRD
ADCON® Gel	2004	32.3%	$4,558,000

ADCON® Gel products are designed to reduce adhesion formation following lumbar spine (ADCON®-L Gel) and peripheral tendon/nerve (ADCON®-T/N Gel) procedures, thus reducing or eliminating post-operative pain. Both ADCON®-L Gel and ADCON®-T/N Gel are commercially available internationally, but are currently not available for sale in the U.S. Our ADCON®-L Gel product had previously received regulatory clearance from the FDA in 1998. In 2000, the FDA determined that the provisions of its Application Integrity Policy (AIP) would be applied to Gliatech due to violations of Good Clinical Practices in the conduct, analysis, and reporting of data specific to the U.S. Clinical Study of ADCON®-L Gel. In 2003, the FDA lifted the AIP status of Gliatech, which subsequently allowed us, as the new owner of the technology, to present the FDA with clinical data intended to support the return of ADCON®-L Gel to the U.S. market. Since the submission of our ADCON®-L Gel PMA application to the FDA in December 2003, we have been working to satisfy additional requirements necessary to obtain FDA approval to market ADCON®-L Gel in the U.S. We will be required to conduct a separate clinical study to enter the U.S. market with ADCON®-T/N Gel.

Our original estimate for receipt of net cash flows associated with this project was in 2004; however, we now anticipate that ADCON®-L Gel will be available for sale in the U.S. market no sooner than 2006. This delay in the estimated completion date has not had a significant impact on our results of operations or financial condition. We expect to pursue necessary clinical studies to allow FDA approval for additional applications outside of the spine, such as the peripheral tendon/nerve. We are unable to estimate at this time when such additional FDA approvals would occur.

We anticipate that portions of our existing cash will be used to continue to develop the acquired IPRD into commercially viable products. This development consists primarily of the completion of all clinical evaluation testing activities and regulatory approvals that are necessary to establish the safety and efficacy of the products and to market them in the U.S. Bringing the acquired IPRD to market also includes testing the products for compatibility and interoperability with commercially viable products. Due to the history of the ADCON® Gel products with the FDA, we are unable to estimate the extent of research and development activities that will be necessary to develop these products into commercially viable products.

We are continuously monitoring our research and development projects. We believe that the assumptions used in the valuation of acquired IPRD represent a reasonably reliable estimate of the future benefits attributable to the acquired IPRD. No assurance can be given that actual results will not deviate from those assumptions in future periods.

Interest expense, net. Our interest expense, net, consists primarily of interest on borrowings outstanding under our senior credit facility and certain of our factoring agreements and is partially offset by interest income of approximately $815,000 and $636,000 in 2004 and 2003, respectively, from our invested cash balances. Our net interest expense also includes non-cash expense associated with the amortization of deferred financing costs resulting from the origination of our senior credit facility of approximately $261,000 during both 2004 and 2003.

Other income, net. Other income, net, primarily consists of gains and losses resulting from foreign currency fluctuations, offset in the second half of 2004 by the impact of gains and losses resulting from certain foreign currency forward contracts. These contracts are discussed further in Note 2 to our consolidated financial statements in this report. Primarily as a result of these forward contracts, our other income, net, decreased from $1.1 million in 2003 to a nominal amount in 2004.

Provision for income taxes. We recorded tax provisions of $13.4 million and $9.7 million in 2004 and 2003, respectively. Our effective tax rate for both 2004 and 2003 was approximately 36%, which reflects the impact of certain tax saving initiatives, including research and development credits and changes in estimates related to the valuation allowances recorded against our deferred tax assets.

During 2004, the American Jobs Creation Act of 2004 (Jobs Creation Act) was signed into law. Beginning in 2005, the Jobs Creation Act includes relief for domestic manufacturers by providing a tax deduction up to 9% of the lesser of qualified production activities income or taxable income. In addition, the Jobs Creation Act also provides for a one-time tax deduction of 85% of certain foreign earnings that are repatriated. Based on our assessment of the repatriation deduction, we have determined to continue our current policy of permanently reinvesting all foreign earnings. With respect to the tax deduction provided for domestic manufacturers, we are in the process of evaluating the potential impact of this portion of the Jobs Creation Act to our business. The transition issues related to this deduction are complex and little interpretative guidance has been issued to date. Accordingly, management has not determined, what, if any, the impact of this tax deduction will have to on our effective tax rate in future periods. Excluding any favorable impact of the Jobs Creation Act, for 2005, we expect our effective tax rate to increase from 2004 to a range of 38% to 39%; however, the actual rate will depend on a number of factors, including the amount of pre-tax income by jurisdiction, any incremental tax saving initiatives that might be identified and implemented and the ultimate impact, if any, of the Jobs Creation Act.

Comparison of the year ended December 31, 2003 to the year ended December 31, 2002

Net sales. Our net sales grew 24% in 2003, totaling $248.9 million. This was attributable to the success of our biologics and extremity product lines, as well as significant growth in our hip product line. Geographically, our domestic net sales totaled $152.9 million in 2003 and $122.4 million in 2002, representing 61% of total net sales in both years and growth of 25%. Our international net sales totaled $96.1 million in 2003, increasing by 22% over net sales of $78.5 million in 2002. Our 2003 international net sales included a favorable currency impact of approximately $11.9 million, principally resulting from the 2003 performance of the euro against the U.S. dollar, when compared to 2002. Our European and Japanese operations were the significant drivers of our sales growth in our international operations in 2003.

From a product line perspective, our net sales growth for 2003 was attributable to increases in sales across all of our principal product lines. For 2003, we experienced growth of 37%, 31%, 26% and 9%, in our hip, biologics, extremity, and knee product lines, respectively. Our most significant growth drivers in 2003 were our hip and biologics product lines. During 2003, our 37% hip sales growth was attributable primarily to demand for our higher-priced CONSERVE® Total Implant with BFH™ Technology, as well as our LINEAGE® Acetabular System and our PROFEMUR® stem products, both of which were positively influenced by the launch of our LINEAGE® ceramic-on-ceramic hip system in the first quarter 2003. Our biologics sales growth of 31%

in 2003 was primarily the result of strong growth across all of our biologics product offerings.

Cost of sales. Our cost of sales as a percentage of net sales decreased slightly to 27.2% in 2003 from 27.7% in 2002. This decrease is primarily a result of our ability to manage certain of our fixed manufacturing costs while our business significantly expanded during 2003.

Operating expenses. Our total operating expenses increased, as a percentage of net sales, by 2.7 percentage points to 61.8% in 2003. Operating expenses include selling, general and administrative expenses, research and development expenses, amortization of intangibles, and stock-based expenses. Additionally, operating expenses included approximately $4.6 million of acquired IPRD costs in 2003 and the favorable impact of our $4.2 million arbitration settlement award in 2002. These two items were the primary drivers of the increase in operating expenses. These amounts were partially offset by favorable selling, general and administrative expenses, resulting from our ability to control our discretionary spending while significantly growing our business, and reductions in amortization of intangible assets.

Provision for income taxes. Our effective tax rate for 2003 was approximately 36% as compared to an effective tax rate of 7% for 2002. Our 2002 effective tax rate was favorably impacted by the reduction of the valuation allowance against our deferred tax assets, which resulted in an $8.1 million non-cash benefit to our provision for income taxes. Excluding this benefit, our effective tax rate for 2002 would have been approximately 37%. The decrease in our effective tax rate in 2003, excluding this benefit, reflected the effect of certain tax savings initiatives that were implemented in 2003.

Seasonal Nature of Business

Our business is seasonal in nature. We traditionally experience lower sales volumes in the third quarter months than throughout the rest of the year as a result of the European holiday schedule during the summer months. In addition, our first quarter selling, general and administrative expenses include additional expenses that we incur in connection with the annual meeting held by the American Academy of Orthopaedic Surgeons. This meeting, which is the largest orthopaedic meeting in the world, features the presentation of scientific papers and instructional courses for orthopaedic surgeons. During this 3-day event, we display our most recent and innovative products for these surgeons.

Liquidity and Capital Resources

The following table sets forth, for the periods indicated, certain liquidity measures (in thousands):

As of December 31,	2004	2003
Cash and cash equivalents	$83,470	$66,571
Working capital	189,466	147,255
Line of credit availability	59,708	57,742

Our cash and cash equivalents increased during 2004 by $16.9 million, compared to an increase of $15.2 million in 2003. Our 2004 increase in cash and cash equivalents is primarily attributable to the generation of $37 million of cash from operating activities during 2004, partially offset by routine capital expenditures. Our 2003 increase in cash and cash equivalents and working capital is primarily attributable to the generation of $40 million of cash from operating activities during 2003, partially offset by capital expenditures and the acquisition of ADCON® Gel technology assets.

Operating Activities. Operating cash flow in 2004 benefited from the profitability of our business and working capital management, which resulted primarily from improved collection of our outstanding receivables during 2004. The improvement in our collections was offset by increased investments in new product inventory during 2004 in order to prepare for anticipated product launches, as well as an increase of approximately $3.9 million in cash tax payments. Operating cash flow in 2003 benefited from the profitability of our business, as well as improved inventory management. Cash generated from operating activities in 2002 totaled approximately $22 million and included the favorable $4.2 million arbitration settlement award, which was partially offset by significant investments in new product inventory

Investing Activities. Our capital expenditures totaled approximately $18.3 million in 2004, $18.1 million in 2003, and $18.0 million in 2002. Our industry is capital intensive, particularly as it relates to surgical instrumentation. Historically, our capital expenditures have consisted of purchased manufacturing equipment, research and testing equipment, computer systems, office furniture and equipment, and surgical instruments. We expect to incur capital expenditures of approximately $30 million in total for 2005 for routine capital expenditures. The increase in anticipated capital spending from 2004 is expected to be primarily attributable to increased investments in surgical instrumentation for new products. Furthermore, we are evaluating our long-term facility needs in the U.S. in response to our anticipated growth. We cannot estimate the amount of capital spending, if any, that will be incurred in 2005 should we expand or construct new facilities.

In 2003, in addition to our routine capital expenditures, we paid $7.8 million to complete the purchase of IPRD, tangible assets, and intangible assets from Gliatech, which were primarily related to the ADCON® Gel technology. We are continuously evaluating opportunities to purchase technology and other forms of intellectual property and are, therefore, unable to predict the timing of future purchases.

Financing Activities. During 2004, we made $4.5 million in scheduled payments related to borrowings under our senior credit facility and approximately $1.8 million in payments related to our long-term capital leases. In the fourth quarter of 2003, our operating subsidiary in Italy began factoring portions of its accounts receivable balances under a new agreement, which is considered a financing transaction for financial reporting purposes. The cash proceeds received from this factoring agreement, net of the amount of factored receivables collected, are reflected as cash flow from financing activities in our consolidated statements of cash flows. In 2004, the net activity under this agreement was consistent as the amount of cash received approximated the receivables collected. We recorded an obligation of $5.2 million and $4.8 million for the amount of receivables factored under this agreement as of December 31, 2004 and 2003, respectively, which is included within "Accrued expenses and other current liabilities" in our consolidated balance sheet. The proceeds received under the agreement in 2004 and 2003

totaled approximately $10.7 million and $4.7 million, respectively. Additionally, we received cash proceeds of $4.1 million from the exercise of stock options and warrants during 2004.

In 2005, our debt payments will increase to $5 million based on the terms of our senior credit facility. Additionally, we will make continued payments under our long-term capital leases, including interest, of approximately $1.6 million. We anticipate that our factoring program in Italy will continue; however, the level and extent of the amounts factored under the agreement and the ultimate amount of proceeds received under the program cannot be predicted. Therefore, we are unable to predict the ultimate amount of proceeds that will be received in 2005 related to this factoring agreement.

Contractual Cash Obligations. At December 31, 2004, we had contractual cash obligations and commercial commitments as follows (in thousands):

Payments Due by Periods	Total	2005	2006-2007	2008 - 2009	After 2009
Amounts reflected in balance sheet:					
Notes payable	$8,750	$5,000	$ 3,750	$ -	$ -
Capital lease obligations[1]	5,032	1,642	2,193	864	333
Amounts not reflected in balance sheet:					
Operating leases	16,150	6,532	7,152	1,004	1,462
Purchase obligations	11,872	6,609	5,263	-	-
Royalty and consulting agreements	15,167	6,266	2,903	1,998	4,000
Total contractual cash obligations	$56,971	$26,049	$21,261	$ 3,866	$5,795

[1] Payments include amounts representing interest

Our senior credit facility, which we entered into in August 2001, has a five-year term and consists of $20 million in term loans, with an unpaid balance of approximately $8.8 million at December 31, 2004, and a revolving loan facility of up to $60 million. Borrowings under the senior credit facility are guaranteed by all of our subsidiaries and collateralized by all of the assets of Wright Medical Technology, Inc., our wholly-owned subsidiary. The credit facility contains customary covenants including, among other things, restrictions on our ability to pay cash dividends, prepay debt, incur additional debt and sell assets. The credit facility also requires us to maintain certain financial covenants, including a specified consolidated leverage (or debt-to-equity) ratio and a specified consolidated fixed charge coverage ratio. In the event that we violate any covenants, we could be required to repay the remaining balance of the debt. Additionally, should we be required to repay the loan before its scheduled maturity, we would incur a charge to operating income for unamortized financing costs. At our option, borrowings under the credit facility bear interest either at a rate equal to a fixed base rate plus a spread of .75% to 1.25% or at a rate equal to an adjusted LIBOR plus a spread of 1.75% to 2.25%, depending on our consolidated leverage ratio, with a current annual rate of 3.625%.

The amounts reflected in the table above for capital lease obligations represent future minimum lease payments under our capital lease agreements which are primarily for certain property and equipment. The present value of the minimum lease payments are recorded in our balance sheet at December 31, 2004. The minimum lease payments related to these leases are discussed further in Note 9 to our consolidated financial statements contained in this report.

The amounts reflected in the table above for operating leases represent future minimum lease payments under noncancellable operating leases primarily for certain equipment and office space. Portions of these payments are denominated in foreign currencies and were translated in the table above based on their respective U.S. dollar exchange rates at December 31, 2004. These future payments are subject to foreign currency exchange rate risk. In accordance with accounting principles generally accepted in the U.S., our operating leases are not recognized in our consolidated balance sheet; however, the minimum lease payments related to these agreements are disclosed in Note 15 to our consolidated financial statements contained in this report.

Our purchase obligations reflected in the table above consist of minimum purchase obligations related to certain supply agreements. The royalty and consulting agreements in the above table represent minimum payments to consultants that are contingent upon future services. Portions of these payments are denominated in foreign currencies and were translated in the table above based on their respective U.S. dollar exchange rates at December 31, 2004. These future payments are subject to foreign currency exchange rate risk. Our purchase obligations and royalty and consulting agreements are disclosed in Note 15 to our consolidated financial statements contained in this report.

In addition to the contractual cash obligations discussed above, all of our domestic sales and a portion of our international sales are subject to commissions based on net sales, and a substantial portion of our global sales are subject to other royalties earned based on product sales. Further, under our factoring agreement in Italy, our liability for cash proceeds received of $5.2 million discussed under the heading, "Financing Activities," may be subject to repayment upon 15 days notice. None of these amounts are included in the table above.

Other Liquidity Information. We have funded our cash needs since 2000

through various equity and debt issuances and through cash flow from operations. In 2001, we completed our IPO of 7,500,000 shares of common stock which generated $84.8 million in net proceeds. In 2002, we completed a secondary offering of 3,450,000 shares of common stock which generated $49.5 million in net proceeds.

Although it is difficult for us to predict our future liquidity requirements, we believe that our current cash balance of approximately $83.5 million, our existing available credit line of approximately $59.7 million, and our expected cash flow from our operating activities, which in 2004 totaled approximately $37.4 million, will be sufficient for the foreseeable future to fund our working capital requirements and operations, permit anticipated capital expenditures in 2005 of approximately $30 million, meet our contractual cash obligations in 2005, and fund any potential expansion of our current facilities or the construction of new facilities.

Critical Accounting Estimates

All of our significant accounting policies and estimates are described in Note 2 to our consolidated financial statements contained in this report. However, certain of our more critical accounting estimates require the application of significant judgment by management in selecting the appropriate assumptions in determining the estimate. By their nature, these judgments are subject to an inherent degree of uncertainty. We develop these judgments based on our historical experience, terms of existing contracts, our observance of trends in the industry, information provided by our customers, and information available from other outside sources, as appropriate. Different, reasonable estimates could have been used in the current period. Additionally, changes in accounting estimates are reasonably likely to occur from period to period. Both of these factors could have a material impact on the presentation of our financial condition, changes in financial condition or results of operations.

We believe that the following financial estimates are both important to the portrayal of our financial condition and results of operations and require subjective or complex judgments. Further, we believe that the items discussed below are properly recorded in the financial statements for all periods presented. Our management has discussed the development, selection, and disclosure of our most critical financial estimates with the audit committee of our Board of Directors and with our independent auditors. The judgments about those financial estimates are based on information available as of the date of the financial statements. Those financial estimates include:

Revenue recognition. Our revenues are generated through two types of customers, hospitals and stocking distributors, with the majority of our revenue derived from sales to hospitals. Our products are sold through a network of independent sales representatives in the U.S. and by a combination of employee sales representatives, independent sales representatives, and stocking distributors outside the U.S. We record revenues from sales to hospitals when the hospital takes title to the product, which is when the product is surgically implanted in a patient and a purchase order is received from the hospital. We view the receipt of a purchase order as the evidence of customer acceptance of the product.

We record revenues from sales to our stocking distributors at the time the product is shipped to the distributor. Our stocking distributors, who sell the products to their customers, take title to the products and assume all risks of ownership. Our distributors are obligated to pay us within specified terms regardless of when, if ever, they sell the products. In general, our distributors do not have any rights of return or exchange; however, in limited situations we have repurchase agreements with certain stocking distributors. Those certain agreements require us to repurchase a specified percentage of the inventory purchased by the distributor within a specified period of time prior to the expiration of the contract. During those specified periods, we defer the applicable percentage of the sales. Approximately $87,000 and $247,000 of deferred revenue related to these types of agreements was recorded at December 31, 2004 and 2003, respectively.

We must make estimates of potential future product returns related to current period product revenue. To do so, we analyze our historical experience related to product returns when evaluating the adequacy of the allowance for sales returns. Judgment must be used and estimates made in connection with establishing the allowance for product returns in any accounting period. Our allowances for product returns of $395,000 and $412,000 are included as a reduction of accounts receivable at December 31, 2004 and 2003, respectively. Should actual future returns vary significantly from our historical averages, our operating results could be affected.

Allowances for doubtful accounts. We experience some credit loss on our accounts receivable and accordingly we must make estimates related to the ultimate collection of our accounts receivable. Specifically, we analyze our accounts receivable, historical bad debt experience, customer concentrations, customer creditworthiness, and current economic trends when evaluating the adequacy of our allowance for doubtful accounts.

The majority of our receivables are from hospitals, many of which are government funded. Accordingly, our collection history with these customers has been favorable. Historically, we have experienced minimal bad debts from our hospital customers and more significant bad debts from certain international distributors, typically as a result of specific financial difficulty or geo-political factors. In 2003 and 2004, the increases in our accounts receivable balance have related almost exclusively to our hospital customers. As the historical bad debt experience with this class of customer is minimal, our allowance has not increased proportionately to the increase in our accounts receivable balance. We write off receivables when we determine that the receivable is uncollectible, typically upon customer bankruptcy or the customer's non-response to collection efforts.

We believe that the amount included in our allowance for doubtful accounts has been a historically accurate estimate of the amount of accounts receivable that are ultimately collected. While we believe that our allowance for doubtful accounts is adequate, the financial condition of our customers and the geo-political factors that impact reimbursement under individual countries' healthcare systems can change rapidly and as such, additional allowances may be required in future periods. Our accounts receivable balance was $61.7 million and $55.8 million, net of allowances for doubtful accounts of $1.8 million and $1.5 million, at December 31, 2004 and 2003, respectively.

Excess and obsolete inventories. We value our inventory at the lower of the actual cost to purchase and/or manufacture the inventory or its net realizable value. We regularly review inventory quantities on hand for excess and obsolete inventory and, when circumstances indicate, we incur charges to write down inventories to their net realizable value. Our review of inventory

for excess and obsolete quantities is based primarily on our estimated forecast of product demand and production requirements for the next twenty-four months. A significant decrease in demand could result in an increase in the amount of excess inventory quantities on hand. Additionally, our industry is characterized by regular new product development that could result in an increase in the amount of obsolete inventory quantities on hand due to cannibalization of existing products. Also, our estimates of future product demand may prove to be inaccurate, in which case we may be required to incur charges for excess and obsolete inventory. In the future, if additional inventory write-downs are required, we would recognize additional cost of goods sold at the time of such determination. Regardless of changes in our estimates of future product demand, we do not increase the value of our inventory above its adjusted cost basis. Therefore, although we make every effort to ensure the accuracy of our forecasts of future product demand, significant unanticipated decreases in demand or technological developments could have a significant impact on the value of our inventory and our reported operating results.

Charges incurred for excess and obsolete inventory were $5.8 million, $2.6 million and $2.8 million for the years ended December 31, 2004, 2003 and 2002, respectively. In 2004, charges incurred for excess and obsolete inventory included $2.4 million recorded to write down certain foot and ankle implant inventory to its net realizable value as a result of our transition to our CHARLOTTE™ Foot and Ankle System.

Goodwill and long-lived assets. We have approximately $8.8 million of goodwill recorded as a result of acquisition of businesses. Goodwill is tested for impairment annually, or more frequently if changes in circumstances or the occurrence of events suggest that impairment exists. We have two reporting units for purposes of evaluating goodwill for impairment, Wright Medical Technology, Inc. (WMT) and Wright Medical Europe (WME). WMT consists of our U.S., Canadian, and Japanese subsidiaries and is primarily consistent with our predecessor company prior its recapitalization. WME consists of our European subsidiaries and is primarily consistent with the former Cremascoli operations prior to its acquisition by us. The annual evaluation of goodwill impairment requires the use of estimates and assumptions to determine the fair value of our reporting units using projections of future cash flows. Our estimates of future sales growth rates and operating margin can significantly affect the outcome of the impairment test. We performed our annual impairment test during the fourth quarter of 2004 and determined that the fair value of our reporting units exceeded the carrying value of those units and, therefore, no impairment charge was necessary.

Our business is capital intensive, particularly as it relates to surgical instrumentation. We depreciate our property, plant and equipment and amortize our intangible assets based upon our estimate of the respective asset's useful life. Our estimate of the useful life of an asset requires us to make judgments about future events, such as product life cycles, new product development, product cannibalization and technological obsolescence, as well as other competitive factors beyond our control. We account for the impairment of long-lived assets in accordance SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets." Accordingly, we evaluate impairments of our property, plant and equipment based upon an analysis of estimated undiscounted future cash flows. If we determine that a change is required in the useful life of an asset, future depreciation/amortization is adjusted accordingly. Alternatively, should we determine that an asset has been impaired, an adjustment would be charged to income based on its fair market value, or discounted cash flows if the fair market value is not readily determinable, reducing income in that period. During 2004, based on our decision to transition to a new line of internally developed foot and ankle products in the first quarter of 2005, we reviewed for impairment our instrumentation related to foot and ankle products sold under a distribution agreement. The projected undiscounted cash flows for these instruments exceeded the carrying value of the instruments and accordingly, no impairment charge was necessary. However, based on our transition to a new product line in the first quarter of 2005, we revised the estimated useful life of these instruments and recorded accelerated depreciation during the fourth quarter of 2004 of approximately $500,000. We expect to record additional accelerated depreciation of approximately $500,000 in the first quarter of 2005.

Product liability claims. Periodically, claims arise involving the use of our products. We make provisions for claims specifically identified for which we believe the likelihood of an unfavorable outcome is probable and an estimate of the amount of loss has been developed. We have recorded at least the minimum estimated liability related to those claims where a range of loss has been established. As additional information becomes available, we reassess the estimated liability related to our pending claims and make revisions as necessary. Future revisions in our estimates of the liability could materially impact our results of operation and financial position. We maintain insurance coverage that limits the severity of any single claim as well as total amounts incurred per policy year, and we believe our insurance coverage is adequate. We use the best information available to us in determining the level of accrued product liabilities and we believe our accruals are adequate. During 2004, we recorded $500,000 in product liability reserves for probable losses following our announcement of a voluntary market withdrawal of a limited number of metal acetabular hip cups intended for use in our CONSERVE® hip systems. Management developed this estimate and believes that the amount recorded is appropriate based on assumptions with respect to estimated patient claims related to the market withdrawal and the acceptance of such claims by our insurer. The nature of a market withdrawal and the associated claims are such that the claims will occur over an extended period of time. Our estimate includes an assumption for unasserted claims based on management's industry experience with similar circumstances. While we believe that the amount recorded related to the market withdrawal is appropriate, it is possible that changes in assumptions related to potential claims or insurance coverage could have an adverse effect on our estimate.

For the years ended December 31, 2003 and 2002, operating expenses were not materially affected by our estimates of product liability claims. Our accrual for product liability claims was approximately $1.0 million and $750,000 at December 31, 2004 and 2003, respectively.

Accounting for income taxes. Our effective tax rate is based on income by tax jurisdiction, statutory rates and tax saving initiatives available to us in the various jurisdictions in which we operate. Significant judgment is required in determining our effective tax rate and evaluating our tax positions. This process includes assessing temporary differences resulting from differing recognition of items for income tax and accounting purposes. These differences result in deferred tax assets and liabilities, which are included

within our consolidated balance sheet. We establish valuation allowances when the amount of future taxable income is not likely to support the recovery of the deferred tax asset. To the extent that we establish a valuation allowance or increase the allowance in a period, we reflect the increase as expense within the tax provision in our statement of operations. In addition to establishing valuation allowances for deferred tax assets, we establish accruals for tax contingencies for certain tax jurisdictions, when, despite our belief that our tax return positions are fully supportable, we believe that certain positions may be challenged and that we may not prevail upon review. We adjust these accruals for tax contingencies in light of changing facts and circumstances, such as the progress of a tax audit. Our tax provision reflects the impact of establishing these accruals for tax contingencies and any subsequent adjustments.

We have recorded valuation allowances of $5.9 million and $16.0 million as of December 31, 2004 and 2003, respectively, due to uncertainties related to our ability to realize, before expiration, some of our deferred tax assets for both U.S. and foreign income tax purposes. These deferred tax assets primarily consist of the carry forward of certain net operating losses and general business tax credits. We established these valuation allowances based on our estimates of taxable income by jurisdiction in which we operate and the period over which our deferred tax assets will be recoverable. In the event that actual results differ from these estimates or we adjust these estimates in future periods, we may need to increase or decrease our valuation allowance, which could materially impact our financial position and results of operations.

We have recorded accruals for tax contingencies of $13.0 million and $7.8 million as of December 31, 2004 and 2003, respectively, for certain exposure items. We established these accruals for tax jurisdictions where we believe that certain positions may be challenged and the likelihood of a favorable outcome upon review is less than probable.

During 2004, we completed certain tax studies. These studies indicated that a revision to our original estimates of the limitations on the utilization of our net operating losses and tax credit carryforwards was required. Accordingly, the completion of the studies resulted in a reduction of approximately $10.7 million in the valuation allowance for these deferred tax assets as the deferred tax assets were more likely than not to be realized in the future. Additionally, these studies indicated that approximately $8.5 million of tax exposure existed as a result of the tax filing positions taken with respect to these net operating losses and tax credit carryforwards. Based on these findings, we reclassified approximately $8.5 million of the valuation allowance to our accruals for tax contingencies. The remaining reduction in our valuation allowance was released through the income tax provision or was a result of currency fluctuations on the portion of our valuation allowances recorded in foreign currencies.

Additionally, in 2004, we favorably resolved certain tax contingencies associated with our December 1999 acquisition of Cremascoli. The favorable resolution of these matters resulted in a reduction of our previously recorded accrual for tax contingencies and goodwill of approximately $3.0 million. Our accruals for tax contingencies are included within "Other liabilities" on our consolidated balance sheet. Additional discussion of our accounting for income taxes is included in Notes 6, 10 and 11 to our consolidated financial statements contained in this report.

Impact of Recently Issued Accounting Pronouncements

In December 2004, the FASB issued SFAS No. 123R, which requires the recognition of compensation expense for the fair value of share-based transactions. We further describe this pronouncement and its anticipated impact on our results of operations under the heading, "Stock based expense" within the "Results of Operations" section of MD&A.

In November 2004, the FASB issued SFAS No. 151, "Inventory Costs - An Amendment of ARB No. 43, Chapter 4" (SFAS No. 151). SFAS No. 151 will no longer allow companies to capitalize inventory costs on their balance sheet when the production defect rate varies significantly from the expected rate. All abnormal freight, handling and material waste will be treated as period expenses. Additionally, SFAS No. 151 requires that a facility's fixed production overhead be charged to inventory based on a range of "normal" capacity. If the production level is abnormally low or high, unallocated overhead should be charged to current period expense. SFAS No. 151 is required to be adopted for annual periods beginning after June 15, 2005; accordingly, we will adopt SFAS No. 151 effective January 1, 2006. We are evaluating the impact of this standard on our results of operations and financial statements.

In December 2004, the FASB issued two FASB Staff Positions (FSP) in response to the Jobs Creation Act related to accounting and disclosures associated with the provisions of the Jobs Creation Act. We further describe the Jobs Creation Act and our evaluation of its impact within the "Results of Operations" section of MD&A. FSP 109-1 requires the deduction for qualified domestic production activities to be accounted for as a special deduction under SFAS No. 109, not as a tax-rate deduction. We will comply with the provisions of FSP 109-1 effective January 1, 2005, should this deduction become available to us. FSP 109-2 allows for additional time for companies to determine whether any foreign earnings will be repatriated under the Jobs Creation Act's one-time deduction for repatriated earnings. Companies that take the additional time are required to provide disclosures about the status of their evaluation. Based on management's assessment of the repatriation deduction, we have determined to continue our current policy of permanently reinvesting all foreign earnings. Therefore, the provisions of FSP 109-2 are not applicable to us.

Factors Affecting Future Operating Results

In addition to the factors described above in MD&A and elsewhere in this report, our future financial results could vary from period to period due to a variety of causes, including the following factors:

We are subject to substantial government regulation that could have a material adverse effect on our business

The production and marketing of our products and our ongoing research and development, preclinical testing and clinical trial activities are subject to extensive regulation and review by numerous governmental authorities both in the U.S. and abroad. U.S. and foreign regulations govern the testing, marketing and registration of new medical devices, in addition to regulating manufacturing practices, reporting, labeling and recordkeeping procedures. The regulatory process requires significant time, effort and

expenditures to bring our products to market, and we cannot be assured that any of our products will be approved. Our failure to comply with applicable regulatory requirements could result in these governmental authorities:

- imposing fines and penalties on us;
- preventing us from manufacturing or selling our products;
- bringing civil or criminal charges against us;
- delaying the introduction of our new products into the market;
- recalling or seizing our products; or
- withdrawing or denying approvals or clearances for our products.

Even if regulatory approval or clearance of a product is granted, this could result in limitations on the uses for which the product may be labeled and promoted. Further, for a marketed product, its manufacturer and manufacturing facilities are subject to periodic review and inspection. Subsequent discovery of problems with a product, manufacturer or facility may result in restrictions on the product, manufacturer or facility, including withdrawal of the product from the market or other enforcement actions.

We are currently conducting clinical studies of some of our products under an IDE. Clinical studies must be conducted in compliance with FDA regulations, or the FDA may take enforcement action. The data collected from these clinical studies will ultimately be used to support market clearance for these products. There is no assurance that the FDA will accept the data from these clinical studies or that it will ultimately allow market clearance for these products.

Our biologics business is subject to emerging governmental regulations that can significantly impact our business

The FDA has statutory authority to regulate allograft-based products, processing and materials. The FDA has been working to establish a more comprehensive regulatory framework for allograft-based products, which are principally derived from cadaveric tissue. The framework developed by the FDA establishes criteria for determining whether a particular human tissue-based product will be classified as human tissue, a medical device or biologic drug requiring premarket clearance or approval. All tissue-based products are subject to extensive FDA regulation, including a requirement that ensures that diseases are not transmitted to tissue recipients. The FDA has also proposed extensive additional regulations that would govern the processing and distribution of all allograft products. Consent to use the donor's tissue must also be obtained. The regulations for allograft-based products are still developing. From time to time, the FDA reviews these products and may informally suggest to us how these products should be classified. If a human tissue-based product is considered human tissue, it does not require FDA clearance or approval before being marketed. If it is considered a medical device or biologic drug, then FDA clearance or approval may be required.

Additionally, our biologics business involves the procurement and transplantation of allograft tissue, which is subject to federal regulation under the National Organ Transplant Act (NOTA). NOTA prohibits the sale of human organs, including bone and other human tissue, for valuable consideration within the meaning of NOTA. NOTA permits the payment of reasonable expenses associated with the transportation, processing, preservation, quality control and storage of human tissue. We currently charge our customers for these expenses. In the future, if NOTA is amended or reinterpreted, we may not be able to charge these expenses to our customers and, as a result, our business could be adversely affected.

Our principal allograft-based biologics offerings include ALLOMATRIX®, GRAFTJACKET®, and IGNITE® products.

Modifications to our marketed devices may require FDA regulatory clearances or approvals or require us to cease marketing or recall the modified devices until such clearances or approvals are obtained

When required, the products we market in the U.S. have obtained premarket notification under Section 510(k) of the Food, Drug and Cosmetic (FDC) Act or were exempt from the 510(k) clearance process. We have modified some of our products and product labeling since obtaining 510(k) clearance, but we do not believe these modifications require us to submit new 510(k) notifications. However, if the FDA disagrees with us and requires us to submit a new 510(k) notification for modifications to our existing products, we may be the subject of enforcement actions by the FDA and be required to stop marketing the products while the FDA reviews the 510(k) notification. If the FDA requires us to go through a lengthier, more rigorous examination than we had expected, our product introductions or modifications could be delayed or canceled, which could cause our sales to decline. In addition, the FDA may determine that future products will require the more costly, lengthy and uncertain PMA application process. Products that are approved through a PMA application generally need FDA approval before they can be modified. See "Business – Government Regulation."

If we lose one of our key suppliers, we may be unable to meet customer orders for our products in a timely manner or within our budget

We rely on a limited number of suppliers for the components used in our products. Our reconstructive joint devices are produced from various surgical grades of titanium, cobalt chrome and stainless steel, various grades of high-density polyethylenes, silicone elastomer and ceramics. We rely on one supplier for the silicone elastomer used in our extremity products. We are aware of only two suppliers of silicone elastomer to the medical device industry for permanent implant usage. Additionally, we rely on one supplier of ceramics for use in our hip products.

In addition, for our biologics products, we depend upon a limited number of sources of DBM and CBM, and any failure to obtain DBM and CBM from these sources in a timely manner will interfere with our ability to process and distribute allograft products. Two not-for-profit tissue banks supplied us with 100% of the DBM and CBM, a key component in the allograft products we currently produce, market and distribute, that we obtained in the U.S. in 2004. We cannot be sure that our supply of DBM and CBM will continue to be available at current levels or will be sufficient to meet our needs, or that our suppliers of DBM and CBM will be free from FDA regulatory action impacting their sale of DBM and CBM. Since there is a small number of suppliers, if we cannot continue to obtain DBM and CBM from these sources in volumes sufficient to meet our needs, we may not be able to locate replacement sources of DBM and CBM on commercially reasonable terms, if at all. This could have the effect of interrupting our business, which could

adversely affect our sales. Further, we rely on one supplier for our GRAFTJACKET® family of soft tissue repair and graft containment products, as well as one supplier for our ADCON® Gel products.

Suppliers of raw materials and components may decide, or be required, for reasons beyond our control to cease supplying raw materials and components to us. FDA regulations may require additional testing of any raw materials or components from new suppliers prior to our use of these materials or components and in the case of a device with a PMA application, we may be required to obtain prior FDA permission, either of which could delay or prevent our access to or use of such raw materials or components.

If we fail to compete successfully in the future against our existing or potential competitors, our sales and operating results may be negatively affected and we may not achieve future growth

The markets for our products are highly competitive and dominated by a small number of large companies. We may not be able to meet the prices offered by our competitors, or offer products similar to or more desirable than those offered by our competitors.

If we are unable to continue to develop and market new products and technologies, we may experience a decrease in demand for our products or our products could become obsolete, and our business would suffer

We are continually engaged in product development and improvement programs, and new products represent a significant component of our growth rate. We may be unable to compete effectively with our competitors unless we can keep up with existing or new products and technologies in the orthopaedic implant market. If we do not continue to introduce new products and technologies, or if those products and technologies are not accepted, we may not be successful. Additionally, our competitors' new products and technologies may beat our products to market, may be more effective or less expensive than our products, or may render our products obsolete.

If our patents and other intellectual property rights do not adequately protect our products, we may lose market share to our competitors and be unable to operate our business profitably

We rely on patents, trade secrets, copyrights, know-how, trademarks, license agreements and contractual provisions to establish our intellectual property rights and protect our products. These legal means, however, afford only limited protection and may not adequately protect our rights. In addition, we cannot be assured that any of our pending patent applications will issue. The U.S. Patent and Trademark Office (USPTO) may deny or require a significant narrowing of the claims in our pending patent applications and the patents issuing from such applications. Any patents issuing from the pending patent applications may not provide us with significant commercial protection. We could incur substantial costs in proceedings before the USPTO. These proceedings could result in adverse decisions as to the priority of our inventions and the narrowing or invalidation of claims in issued patents. In addition, the laws of some of the countries in which our products are or may be sold may not protect our intellectual property to the same extent as U.S. laws or at all. We also may be unable to protect our rights in trade secrets and unpatented proprietary technology in these countries.

In addition, we hold licenses from third parties that are necessary to utilize certain technologies used in the design and manufacturing of some of our products. The loss of such licenses would prevent us from manufacturing, marketing and selling these products, which could harm our business.

We seek to protect our trade secrets, know-how and other unpatented proprietary technology, in part, with confidentiality agreements with our employees, independent distributors and consultants. We cannot be assured, however, that the agreements will not be breached, adequate remedies for any breach would be available, or our trade secrets, know-how, and other unpatented proprietary technology will not otherwise become known to or independently developed by our competitors.

If we lose any existing or future intellectual property lawsuits, a court could require us to pay significant damages or prevent us from selling our products

The medical device industry is litigious with respect to patents and other intellectual property rights. Companies in the medical device industry have used intellectual property litigation to gain a competitive advantage. We are currently involved in an intellectual property lawsuit with Howmedica Osteonics Corp., a subsidiary of Stryker Corporation, where it is alleged that our ADVANCE® Knee product line infringes one of Howmedica's patents. See "Legal Proceedings" for more information regarding this lawsuit. If Howmedica were to succeed in obtaining the relief it claims, the court could award damages to Howmedica and impose an injunction against further sales of our product. If a monetary judgment is rendered against us, we may be forced to raise or borrow funds, as a supplement to any available insurance claim proceeds, to pay the damages award.

In the future, we may become a party to other lawsuits involving patents or other intellectual property. A legal proceeding, regardless of the outcome, could drain our financial resources and divert the time and effort of our management. If we lose one of these proceedings, a court, or a similar foreign governing body, could require us to pay significant damages to third parties, require us to seek licenses from third parties and pay ongoing royalties, require us to redesign our products, or prevent us from manufacturing, using or selling our products. In addition to being costly, protracted litigation to defend or prosecute our intellectual property rights could result in our customers or potential customers deferring or limiting their purchase or use of the affected products until resolution of the litigation.

If product liability lawsuits are brought against us, our business may be harmed

The manufacture and sale of medical devices exposes us to significant risk of product liability claims. In the past, we have had a number of product liability claims relating to our products, none of which either individually, or in the aggregate, have resulted in a material negative impact on our business. In the future, we may be subject to additional product liability claims, some of which may have a negative impact on our business. Additionally, we could experience a material design or manufacturing failure in our products, a quality system failure, other safety issues, or heightened regulatory scrutiny

that would warrant a recall of some of our products. Our existing product liability insurance coverage may be inadequate to protect us from any liabilities we might incur. If a product liability claim or series of claims is brought against us for uninsured liabilities or in excess of our insurance coverage, our business could suffer. In addition, a recall of some of our products, whether or not the result of a product liability claim, could result in significant costs and loss of customers.

Fluctuations in insurance expense could adversely affect our profitability

We hold a number of insurance policies, including product liability insurance, directors' and officers' liability insurance, property insurance and workers' compensation insurance. In recent years, our industry has experienced significant increases in product liability insurance premiums. If the costs of maintaining adequate insurance coverage should increase significantly in the future, our operating results could be materially adversely impacted.

If we cannot retain our key personnel, we will not be able to manage and operate successfully and we may not be able to meet our strategic objectives

Our continued success depends, in part, upon key managerial, scientific, sales and technical personnel, as well as our ability to continue to attract and retain additional highly qualified personnel. We compete for such personnel with other companies, academic institutions, governmental entities and other organizations. There can be no assurance that we will be successful in retaining our current personnel or in hiring or retaining qualified personnel in the future. Loss of key personnel or the inability to hire or retain qualified personnel in the future could have a material adverse effect on our ability to operate successfully. Further, our ability to enforce non-compete arrangements related to key personnel who have left the business could have a material adverse effect on our business.

We derive a significant portion of our sales from operations in international markets that are subject to political, economic and social instability

We derive a significant portion of our sales from operations in international markets. Our international distribution system consists of 7 direct sales offices and 89 stocking distribution partners, which combined employ approximately 400 sales representatives who sell in over 60 countries. Most of these countries are, to some degree, subject to political, social and economic instability. For the years ended December 31, 2004 and 2003, approximately 39% of our net sales were derived from our international operations. Our international sales operations expose us and our representatives, agents and distributors to risks inherent in operating in foreign jurisdictions. These risks include:

- the imposition of additional foreign governmental controls or regulations on orthopaedic implants and biologics products;
- new export license requirements, particularly related to our biologics products;
- economic instability, including currency risk between the U.S. dollar and foreign currencies, in our target markets;
- a shortage of high-quality international salespeople and distributors;
- loss of any key personnel who possess proprietary knowledge or are otherwise important to our success in international markets;
- changes in third-party reimbursement policy that may require some of the patients who receive our implant products to directly absorb medical costs or that may necessitate our reducing selling prices for our products;
- changes in tariffs and other trade restrictions, particularly related to the exportation of our biologics products;
- work stoppages or strikes in the health care industry, such as those that have previously affected our operations in France, Canada, Korea and Finland in the past;
- a shortage of nurses in some of our target markets, particularly affecting our operations in France; and
- exposure to different legal and political standards due to our conducting business in over 60 countries.

Any material decrease in our foreign sales would negatively impact our profitability. Our international sales are predominately generated in Europe. In Europe, health care regulation and reimbursement for medical devices vary significantly from country to country. This changing environment could adversely affect our ability to sell our products in some European countries.

Our business could suffer if the medical community does not continue to accept allograft technology

New allograft products, technologies and enhancements may never achieve broad market acceptance due to numerous factors, including:

- lack of clinical acceptance of allograft products and related technologies;
- the introduction of competitive tissue repair treatment options that render allograft products and technologies too expensive and obsolete;
- lack of available third-party reimbursement;
- the inability to train surgeons in the use of allograft products and technologies;
- the risk of disease transmission; and
- ethical concerns about the commercial aspects of harvesting cadaveric tissue.

Market acceptance will also depend on the ability to demonstrate that existing and new allografts and technologies are attractive alternatives to existing tissue repair treatment options. To demonstrate this, we rely upon surgeon evaluations of the clinical safety, efficacy, ease of use, reliability and cost effectiveness of our tissue repair options and technologies. Recommendations and endorsements by influential surgeons are important to the commercial success of allograft products and technologies. In addition, several countries, notably Japan, prohibit the use of allografts. If allograft products and technologies are not broadly accepted in the marketplace, we may not achieve a competitive position in the market.

If adequate levels of reimbursement from third-party payors for our products are not obtained, surgeons and patients may be reluctant to use our products and our sales may decline

In the U.S., health care providers that purchase our products generally rely on third-party payors, principally federal Medicare, state Medicaid and private health insurance plans, to pay for all or a portion of the cost of joint reconstructive procedures and products utilized in those procedures. We may be unable to sell our products on a profitable basis if third-party payors deny coverage or reduce their current levels of reimbursement. Our sales depend largely on governmental health care programs and private health insurers reimbursing patients' medical expenses. Surgeons, hospitals and other health care providers may not purchase our products if they do not receive satisfactory reimbursement from these third-party payors for the cost of the procedures using our products. Payors continue to review their coverage policies carefully for existing and new therapies and can, without notice, deny coverage for treatments that include the use of our products.

In addition, some health care providers in the U.S. have adopted or are considering a managed care system in which the providers contract to provide comprehensive heath care for a fixed cost per person. Health care providers may attempt to control costs by authorizing fewer elective surgical procedures, including joint reconstructive surgeries, or by requiring the use of the least expensive implant available.

If adequate levels of reimbursement from third-party payors outside of the U.S. are not obtained, international sales of our products may decline. Outside of the U.S., reimbursement systems vary significantly by country. Many foreign markets have government-managed health care systems that govern reimbursement for medical devices and procedures. Canada, and some European and Asian countries, in particular France, Japan, Taiwan, and Korea, have tightened reimbursement rates. Additionally, some foreign reimbursement systems provide for limited payments in a given period and therefore result in extended payment periods.

If market clearance is not obtained for the re-launch of the ADCON® Gel products and the launch of the CONSERVE® Plus implant in the U.S., growth of our biologics and hip product lines could be impacted

Our ADCON® Gel products and our CONSERVE® Plus Resurfacing Implant are available outside the U.S. and are pending FDA clearance for the U.S. market. There can be no assurance that the sale of our ADCON® Gel or CONSERVE® Plus products in the U.S. will be cleared by the FDA in a timely manner or at all, which could have a significant impact on the future growth of our biologics and hip product lines, respectively.

If surgeons do not recommend and endorse our products, our sales may decline or we may be unable to increase our sales and profits

In order for us to sell our products, surgeons must recommend and endorse them. We may not obtain the necessary recommendations or endorsements from surgeons. Acceptance of our products depends on educating the medical community as to the distinctive characteristics, perceived benefits, clinical efficacy and cost-effectiveness of our products compared to products of our competitors and on training surgeons in the proper application of our products.

If a natural or man-made disaster strikes our manufacturing facilities, we could be unable to manufacture our products for a substantial amount of time and our sales could decline

We have relied to date principally on our manufacturing facilities in Arlington, Tennessee, and Toulon, France. These facilities and the manufacturing equipment we use to produce our products would be difficult to replace and could require substantial lead-time to repair or replace. Our facilities may be affected by natural or man-made disasters. In the event one of our facilities was affected by a disaster, we would be forced to rely on third-party manufacturers or shift production to our other manufacturing facility. Although we believe we possess adequate insurance for damage to our property and the disruption of our business from casualties, such insurance may not be sufficient to cover all of our potential losses and may not continue to be available to us on acceptable terms or at all.

Our business plan relies on certain assumptions about the market for our products, which, if incorrect, may adversely affect our profitability

We believe that the aging of the general population and increasingly active lifestyles will continue and that these trends will increase the need for our orthopaedic implant products. The projected demand for our products could materially differ from actual demand if our assumptions regarding these trends and acceptance of our products by the medical community prove to be incorrect or do not materialize, or if non-surgical treatments gain more widespread acceptance as a viable alternative to orthopaedic implants.

Fluctuations in foreign currency exchange rates could result in declines in our reported sales and earnings

Since a majority of our international sales are denominated in local currencies and not in U.S. dollars, our reported sales and earnings are subject to fluctuations in foreign exchange rates. Our international net sales were favorably affected by the impact of foreign currency fluctuations totaling $8.1 million in 2004 and $11.9 million in 2003. During the second half of 2004, we began a derivative program using 30-day foreign currency forward contracts to mitigate the risk of currency fluctuations on our intercompany receivable and payable balances that are denominated in foreign currencies. These forward contracts are expected to offset the transactional gains and losses on the related intercompany balances. These forward contracts are not designated as hedging instruments under SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities." Accordingly, the changes in the fair value and the settlement of the contracts are recognized in the period incurred.

Efforts to acquire and integrate other companies or product lines could adversely affect our operations and financial results

We may pursue acquisitions of other companies or product lines. Our ability to grow through acquisitions depends upon our ability to identify, negotiate, complete and integrate suitable acquisitions and to obtain any necessary financing. Even if we complete acquisitions, we may also experience:

- difficulties in integrating any acquired companies, personnel and products into our existing business;
- delays in realizing the benefits of the acquired company or products;
- diversion of our management's time and attention from other business concerns;
- limited or no direct prior experience in new markets or countries we may enter;

- higher costs of integration than we anticipated; or
- difficulties in retaining key employees of the acquired business who are necessary to manage these acquisitions.

In addition, an acquisition could materially impair our operating results by causing us to incur debt or requiring us to amortize acquisition expenses and acquired assets.

Our quarterly operating results are subject to substantial fluctuations and you should not rely on them as an indication of our future results

Our quarterly operating results may vary significantly due to a combination of factors, many of which are beyond our control. These factors include:

- demand for products, which historically has been lowest in the third quarter;
- our ability to meet the demand for our products;
- increased competition;
- the number, timing and significance of new products and product introductions and enhancements by us and our competitors;
- our ability to develop, introduce and market new and enhanced versions of our products on a timely basis;
- changes in pricing policies by us and our competitors;
- changes in the treatment practices of orthopaedic surgeons;
- changes in distributor relationships and sales force size and composition;
- the timing of material expense- or income-generating events and the related recognition of their associated financial impact;
- the timing of significant orders and shipments;
- availability of raw materials;
- work stoppages or strikes in the health care industry;
- changes in FDA and foreign governmental regulatory policies, requirements and enforcement practices;
- changes in accounting policies, estimates, and treatments; and
- general economic factors.

We believe that our quarterly sales and operating results may vary significantly in the future and that period-to-period comparisons of our results of operations are not necessarily meaningful and should not be relied upon as indications of future performance. We cannot assure you that our sales will increase or be sustained in future periods or that we will be profitable in any future period. Any shortfalls in sales or earnings from levels expected by securities or orthopaedic industry analysts could have an immediate and significant adverse effect on the trading price of our common stock in any given period.

We rely on our independent sales distributors and sales representatives to market and sell our products

Our success depends largely upon marketing arrangements with independent sales distributors and sales representatives, in particular their sales and service expertise and relationships with the customers in the marketplace. Independent distributors and sales representatives may terminate their relationships with us or devote insufficient sales efforts to our products. We do not control our independent distributors and they may not be successful in implementing our marketing plans. Our failure to maintain our existing relationships with our independent distributors and sales representatives could have an adverse effect on our operations. Similarly, our failure to recruit and retain additional skilled independent sales distributors and sales representatives could have an adverse effect on our operations. We have experienced turnover with some of our independent distributors in the past which adversely affected short-term financial results while we transitioned to new independent distributors. While we believe these transitions have been managed effectively, similar occurrences could happen in the future with different results which could have a greater adverse effect on our operations than we have previously experienced.

Market Risk Sensitive Instruments and Positions

Interest Rate Risk. Our exposure to interest rate risk arises principally from the variable rates associated with our credit facility. On December 31, 2004, we had borrowings of $8.8 million under our credit facility which are subject to a variable interest rate, with a current annual rate of 3.625%. The carrying value of these borrowings approximates fair value due to the variable rate. Based on this debt level, a 10% increase in the interest rate of all such borrowings would cause us to incur an increase in interest expense of approximately $32,000 on an annual basis. We currently do not hedge our exposure to interest rate fluctuations, but may do so in the future.

Foreign Currency Rate Fluctuations. Fluctuations in the rate of exchange between the U.S. dollar and foreign currencies could adversely affect our financial results. Approximately 33% of our total net sales were denominated in foreign currencies during the year ended December 31, 2004. We expect that foreign currencies will continue to represent a similarly significant percentage of our net sales in the future. Costs related to these sales are largely denominated in the same respective currencies, thereby limiting our transaction risk exposures. However, for sales not denominated in U.S. dollars, if there is an increase in the rate at which a foreign currency is exchanged for U.S. dollars, it will require more of the foreign currency to equal a specified amount of U.S. dollars than before the rate increase. In such cases, if we price our products in the foreign currency, we will receive less in U.S. dollars than we did before the rate increase went into effect. If we price our products in U.S. dollars and competitors price their products in local currency, an increase in the relative strength of the U.S. dollar could result in our prices not being competitive in a market where business is transacted in the local currency.

A substantial majority of our sales denominated in foreign currencies are derived from European Union countries and are denominated in the euro. Additionally, we have significant intercompany receivables from our foreign subsidiaries which are denominated in foreign currencies, principally the euro and the Japanese yen. Our principal exchange rate risk, therefore, exists between the U.S. dollar and the euro and the U.S. dollar and the yen. Fluctuations from the beginning to the end of any given reporting period result in the revaluation of our foreign currency-denominated intercompany receivables and payables, generating currency translation gains or losses that impact our non-operating income/expense levels in the respective period. As discussed in Note 2 to our consolidated financial statements in Item 8 of this report, during the second half of 2004, we entered into certain

short-term derivative financial instruments in the form of foreign currency forward contracts. These forward contracts are designed to mitigate our exposure to currency fluctuations in our intercompany balances denominated in euros, Japanese yen and Canadian dollars. Any change in the fair value of these forward contracts as a result of a fluctuation in a currency exchange rate is expected to be offset by a change in the value of the intercompany balance. These contracts are effectively closed at the end of each reporting period.

Safe-Harbor Statement

This annual report contains "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. All statements made in this annual report, other than statements of historical fact, are forward-looking statements. Forward-looking statements reflect management's current knowledge, assumptions, beliefs, estimates, and expectations and express management's current views of future performance, results, and trends. We wish to caution readers that actual results might differ materially from those described in the forward-looking statements. Forward-looking statements are subject to a number of risks and uncertainties, including the factors discussed in our filings with the Securities and Exchange Commission (including those described within the "Factors Affecting Future Operating Results" section of MD&A and elsewhere in this annual report), which could cause our actual results to differ materially from those described in the forward-looking statements. Although we believe that the forward-looking statements are accurate, there can be no assurance that any forward-looking statement will prove to be accurate. A forward-looking statement should not be regarded as a representation by us that the results described therein will be achieved. We wish to caution readers not to place undue reliance on any forward-looking statement. The forward-looking statements are made as of the date of this annual report, and we assume no obligation to update any forward-looking statement after this date.

Wright Medical Group, Inc. Consolidated Balance Sheets
(in thousands, except share data)

December 31,	2004	2003
Assets:		
Current assets:		
Cash and cash equivalents	$83,470	$66,571
Accounts receivable, net	61,662	55,821
Inventories	76,269	64,204
Prepaid expenses	4,822	5,046
Deferred income taxes	24,082	15,591
Other current assets	4,717	3,291
Total current assets	255,022	210,524
Property, plant and equipment, net	70,207	66,915
Goodwill	8,845	11,248
Intangible assets, net	17,140	18,646
Deferred income taxes	8,873	13,398
Other assets	1,071	1,372
Total assets	$361,158	$322,103
Liabilities and Stockholders' Equity:		
Current liabilities:		
Accounts payable	$13,969	$14,227
Accrued expenses and other current liabilities	45,256	42,814
Current portion of long-term obligations	6,331	6,228
Total current liabilities	65,556	63,269
Long-term obligations	5,952	11,096
Deferred income taxes	26	1,203
Other liabilities	13,555	8,217
Total liabilities	85,089	83,785
Commitments and contingencies (Note 15)		
Stockholders' equity:		
Common stock, voting, $.01 par value, shares authorized - 100,000,000; shares issued and outstanding – 33,850,202 in 2004, 33,040,747 in 2003	339	330
Additional paid-in capital	269,944	263,455
Deferred compensation	(188)	(1,452)
Accumulated other comprehensive income	21,642	15,675
Accumulated deficit	(15,668)	(39,690)
Total stockholders' equity	276,069	238,318
	$361,158	$322,103

The accompanying notes are an integral part of these consolidated financial statements.

Wright Medical Group, Inc. Consolidated Statements of Operations
(in thousands, except per share data)

Year Ended December 31,	2004	2003	2002
Net sales	$297,539	$248,932	$200,873
Cost of sales	84,183	67,815	55,616
Gross profit	213,356	181,117	145,257
Operating expenses:			
Selling, general and administrative	151,144	127,612	106,875
Research and development	18,421	16,151	10,357
Amortization of intangible assets	3,889	3,562	3,946
Stock-based expense[1]	1,489	2,068	1,724
Acquired in-process research and development costs	-	4,558	-
Arbitration settlement award	-	-	(4,200)
Total operating expenses	174,943	153,951	118,702
Operating income	38,413	27,166	26,555
Interest expense, net	1,064	1,107	938
Other income, net	(74)	(1,060)	(1,277)
Income before income taxes	37,423	27,119	26,894
Provision for income taxes	13,401	9,722	1,834
Net income	$24,022	$17,397	$25,060
Net income per share (Note 8):			
Basic	$0.72	$0.53	$0.79
Diluted	$0.68	$ 0.50	$ 0.75
Weighted-average number of common shares outstanding – basic	33,391	32,857	31,870
Weighted-average number of common shares outstanding – diluted	35,317	34,561	33,550

[1] Amounts presented as stock-based expense consist of; cost of sales totaling $68, $107, and $108 for the years ended December 31, 2004, 2003, and 2002 respectively; selling, general and administrative expenses of $1,364, $1,875, and $1,506 for the years ended December 31, 2004, 2003, and 2002, respectively; and research and development expenses of $57, $86, and $110 for the years ended December 31, 2004, 2003, and 2002, respectively.

The accompanying notes are an integral part of these consolidated financial statements.

Wright Medical Group, Inc. Consolidated Statements of Cash Flows
(in thousands)

Year Ended December 31,	2004	2003	2002
Operating activities:			
Net Income	$24,022	$17,397	$25,060
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation	17,278	13,948	13,553
Amortization of deferred financing costs	261	261	261
Amortization of intangible assets	3,889	3,562	3,946
Deferred income taxes	5,068	4,565	946
Stock-based expenses	1,489	2,068	1,724
In-process research and development costs	-	4,558	-
Other	623	275	900
Changes in assets and liabilities, net of acquisitions:			
Accounts receivable	(3,811)	(11,359)	(4,653)
Inventories	(7,861)	(3,466)	(12,242)
Other current assets	(3,223)	(676)	(2,596)
Accounts payable	(849)	3,153	509
Accrued expenses and other liabilities	479	5,779	(5,458)
Net cash provided by operating activities	37,365	40,065	21,950
Investing activities:			
Capital expenditures	(18,316)	(18,116)	(17,974)
Purchase of tangible and intangible assets (Note 3)	(161)	(7,799)	(4,469)
Other	49	71	13
Net cash used in investing activities	(18,428)	(25,844)	(22,430)
Financing activities:			
Issuance of common stock	4,056	1,678	52,347
Financing under factoring agreements, net	(29)	4,680	-
Payments of bank and other financing	(6,332)	(5,844)	(3,963)
Net cash (used in) provided by financing activities	(2,305)	514	48,384
Effect of exchange rates on cash and cash equivalents	267	463	699
Net increase in cash and cash equivalents	16,899	15,198	48,603
Cash and cash equivalents, beginning of period	66,571	51,373	2,770
Cash and cash equivalents, end of period	$83,470	$ 66,571	$51,373

The accompanying notes are an integral part of these consolidated financial statements.

Wright Medical Group, Inc. Consolidated Statement of Changes in Stockholders' Equity and Comprehensive Income
For the Year Ended December 31, 2002
(in thousands, except share data)

	Common Stock, Voting		Common Stock, Non-voting						
	No. of Shares	Amount	No. of Shares	Amount	Additional Paid-in Capital	Accumulated Deficit	Deferred Compensation	Accumulated Other Comprehensive Income (Loss)	Total Stockholders' Equity
Balance at December 31, 2001	23,257,532	$ 233	5,288,595	$ 53	$207,197	$ (82,147)	$ (4,798)	$ (3,238)	$ 117,300
2002 Activity:									
Net income	-	-	-	-	-	25,060	-	-	25,060
Foreign currency translation	-	-	-	-	-	-	-	7,521	7,521
Total comprehensive income									32,581
Issuance of common stock, net of costs	4,166,247	41	-	-	52,306	-	-	-	52,347
Tax benefit of employee stock option exercises	-	-	-	-	1,047	-	-	-	1,047
Conversion of non-voting common stock to voting common stock	5,288,595	53	(5,288,595)	(53)	-	-	-	-	-
Deferred stock-based compensation	-	-	-	-	90	-	(90)	-	-
Stock-based compensation	-	-	-	-	-	-	1,724	-	1,724
Balance at December 31, 2002	32,712,374	$ 327	-	-	$260,640	$ (57,087)	$ (3,164)	$ 4,283	$ 204,999

The accompanying notes are an integral part of these consolidated financial statements.

Wright Medical Group, Inc. Consolidated Statements of Changes in Stockholders' Equity and Comprehensive Income For the Years Ended December 31, 2003 and 2004

(in thousands, except share data)

	Common Stock, Voting						
	No.of Shares	Amount	Additional Paid-in Capital	Accumulated Deficit	Deferred Compensation	Accumulated Other Comprehensive Income	Total Stockholders' Equity
Balance at December 31, 2002	32,712,374	$ 327	$260,640	$(57,087)	$(3,164)	$4,283	$204,999
2003 Activity:							
Net income	-	-	-	17,397	-	-	17,397
Foreign currency translation	-	-	-	-	-	11,392	11,392
Total comprehensive income							28,789
Issuance of common stock, net of costs	328,373	3	1,675	-	-	-	1,678
Tax benefit of employee stock option exercises	-	-	784	-	-	-	784
Deferred stock-based compensation	-	-	593	-	(593)	-	-
Stock-based compensation	-	-	-	-	2,068	-	2,068
Forfeiture of stock options	-	-	(237)	-	237	-	-
Balance at December 31, 2003	33,040,747	$ 330	$263,455	$(39,690)	$(1,452)	$ 15,675	$238,318
2004 Activity:							
Net income	-	-	-	24,022	-	-	24,022
Foreign currency translation	-	-	-	-	-	5,967	5,967
Total comprehensive income							29,989
Issuance of common stock, net of costs	809,455	9	4,047	-	-	-	4,056
Tax benefit of employee stock option exercises	-	-	2,217	-	-	-	2,217
Deferred stock-based compensation	-	-	331	-	(331)	-	-
Stock-based compensation	-	-	-	-	1,489	-	1,489
Forfeiture of stock options	-	-	(106)	-	106	-	-
Balance at December 31, 2004	33,850,202	$339	$269,944	$(15,668)	$(188)	$21,642	$276,069

The accompanying notes are an integral part of these consolidated financial statements.

1. Organization and Description of Business:

Wright Medical Group, Inc. (the "Company"), through Wright Medical Technology, Inc. and other operating subsidiaries, is a global medical device company specializing in the design, manufacture and marketing of reconstructive joint devices and biologics products. The Company's products are sold through a network of independent sales representatives in the U.S. and by a combination of employee sales representatives, independent sales representatives, and stocking distributors outside the U.S. The Company promotes its products in over 60 countries with principal markets of the U.S., Europe, and Japan. The Company is headquartered in suburban Memphis, Tennessee.

The Company was incorporated on November 23, 1999 as a Delaware corporation (previously named Wright Acquisition Holdings, Inc.) and had no operations until an investment group led by Warburg, Pincus Equity Partners, L.P. ("Warburg") acquired majority ownership of Wright Medical Technology, Inc. (the "Predecessor Company") on December 7, 1999. This transaction, which represents a recapitalization of the Predecessor Company and the inception of the Company in its present form, was accounted for using the purchase method of accounting.

On December 22, 1999 the Company acquired all of the outstanding common stock of Cremascoli Ortho Holding, S.A. ("Cremascoli"), an orthopaedic medical device company headquartered in Toulon, France. The acquisition was accounted for using the purchase method of accounting and, accordingly, the results of operations of Cremascoli have been included in the Company's consolidated financial statements from the date of acquisition.

On July 18, 2001, the Company completed its initial public offering (the "IPO"), issuing 7,500,000 shares of common stock which generated net proceeds of $84.8 million. On March 6, 2002, the Company and certain selling stockholders completed a secondary offering which generated net proceeds of $49.5 million.

2. Summary of Significant Accounting Policies:

Principles of Consolidation. The accompanying consolidated financial statements include the accounts of the Company and its wholly owned domestic and international subsidiaries. All significant intercompany accounts and transactions have been eliminated in consolidation.

Use of Estimates. The preparation of financial statements in conformity with accounting principles generally accepted in the United States ("U.S.") requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates. The most significant areas requiring the use of management estimates relate to revenue recognition, the determination of allowances for doubtful accounts, excess and obsolete inventories, accounting for goodwill and long-lived assets, product liability claims and accounting for income taxes.

Cash and Cash Equivalents. Cash and cash equivalents include all cash balances and short-term investments with original maturities of three months or less.

Inventories. The Company's inventories are valued at the lower of cost or market on a first-in, first-out ("FIFO") basis. Inventory costs include material, labor costs and manufacturing overhead. The Company regularly reviews inventory quantities on hand for excess and obsolete inventory and, when circumstances indicate, the Company incurs charges to write down inventories to their net realizable value. The Company's review of inventory for excess and obsolete quantities is based primarily on its estimated forecast of product demand and production requirements for the next twenty-four months. Charges incurred for excess and obsolete inventory were $5.8 million, $2.6 million and $2.8 million for the years ended December 31, 2004, 2003 and 2002, respectively. In 2004, charges incurred for excess and obsolete inventory included $2.4 million recorded to write down certain foot and ankle implant inventory to its net realizable value, as a result of the Company's transition to the CHARLOTTE™ Foot and Ankle System.

Product Liability Claims. The Company makes provisions for claims specifically identified for which it believes the likelihood of an unfavorable outcome is probable and an estimate of the amount of loss has been developed. The Company has recorded at least the minimum estimated liability related to those claims where a range of loss has been established. The Company's accrual for product liability claims was approximately $1.0 million and $750,000 at December 31, 2004 and 2003, respectively.

Property, Plant and Equipment. The Company's property, plant and equipment is stated at cost. Depreciation, which includes amortization of assets under capital lease, is provided on a straight-line basis over the estimated useful lives based on the following categories:

Land improvements	15 to 25 years
Buildings	10 to 45 years
Machinery and equipment	3 to 20 years
Furniture, fixtures and office equipment	1 to 14 years
Instruments	5 to 6 years

Expenditures for major renewals and betterments that extend the useful life of the assets are capitalized. Maintenance and repair costs are charged to expense as incurred. Upon sale or retirement, the asset cost and related accumulated depreciation are eliminated from the respective accounts and any resulting gain or loss is included in income.

Intangible Assets and Goodwill. Goodwill is recognized for the excess of the purchase price over the fair value of assets of businesses acquired. Goodwill is required to be tested for impairment at least annually. Unless circumstances otherwise dictate, we perform our annual impairment test in the fourth quarter. Accordingly, during the fourth quarter of 2004, the Company evaluated goodwill for impairment and determined that the fair values of its reporting units exceeded their carrying values, indicating that goodwill was not impaired. The Company has two reporting units for purposes of evaluating goodwill for impairment, Wright Medical Technology, Inc. ("WMT") and Wright Medical Europe ("WME"). WMT consists of the Company's U.S., Canadian, and Japanese subsidiaries, and is primarily consistent with the Predecessor Company prior its recapitalization. WME consists of the Company's European subsidiaries and is primarily consistent with the former Cremascoli operations prior to its acquisition by the Company.

The Company's intangible assets with estimable useful lives are amortized over their respective estimated useful lives to their estimated residual values, and are reviewed for impairment in accordance with Statement of Financial

Accounting Standards ("SFAS") No. 144, *"Accounting for Impairment or Disposal of Long-Lived Assets."* The Company amortizes intangible assets on a straight line basis over their estimated useful lives. The weighted average amortization periods for completed technology, distribution channels, trademarks and licenses are 8 years, 10 years, 9 years, and 5 years, respectively. The weighted average amortization period of the Company's intangible assets on a combined basis is 9 years.

Valuation of Long-Lived Assets. Management periodically evaluates carrying values of long-lived assets, including property, plant and equipment and intangible assets, when events and circumstances indicate that these assets may have been impaired. The Company accounts for the impairment of long-lived assets in accordance SFAS No. 144, *"Accounting for the Impairment or Disposal of Long-Lived Assets."* Accordingly, the Company evaluates impairment of its property, plant and equipment based upon an analysis of estimated undiscounted future cash flows. If it is determined that a change is required in the useful life of an asset, future depreciation/amortization is adjusted accordingly. Alternatively, should the Company determine that an asset is impaired, an adjustment would be charged to income based on its fair market value, or discounted cash flows if the fair market value is not readily determinable, reducing income in that period.

Allowances for Doubtful Accounts. The Company experiences some credit loss on its accounts receivable and accordingly it must make estimates related to the ultimate collection of its accounts receivable. Specifically, management analyzes the Company's accounts receivable, historical bad debt experience, customer concentrations, customer credit-worthiness, and current economic trends, when evaluating the adequacy of its allowance for doubtful accounts.

The majority of the Company's receivables are from hospitals, many of which are government funded. Accordingly, the Company's collection history with this class of customer has been favorable. Historically, the Company has experienced minimal bad debts from its hospital customers and more significant bad debts from certain international distributors, typically as a result of specific financial difficulty or geo-political factors. In 2003 and 2004, the increases in the Company's accounts receivable balance have related almost exclusively to its hospital customers. As the historical bad debt experience with this class of customer is minimal, the allowance has not increased proportionately to the increase in the accounts receivable balance. The Company writes off receivables when it determines that the receivables are uncollectible, typically upon customer bankruptcy or the customer's non-response to collection efforts. The Company's allowance for doubtful accounts totaled $1.8 million and $1.5 million at December 31, 2004 and 2003, respectively.

Concentrations of Supply of Raw Material. The Company relies on a limited number of suppliers for the components used in the Company's products. The Company's reconstructive joint devices are produced from various surgical grades of titanium, cobalt chrome and stainless steel, various grades of high-density polyethylenes, silicone elastomer and ceramics. The Company relies on one supplier for the silicone elastomer used in the Company's extremity products. The Company is aware of only two suppliers of silicone elastomer to the medical device industry for permanent implant usage. Further, the Company relies on one supplier of ceramics for use in the Company's hip products. In addition, for the Company's biologics products, it depends on a limited number of sources of demineralized bone matrix ("DBM") and cancellous bone matrix ("CBM"). Two not-for-profit tissue banks supplied the Company with all of the DBM and CBM that it used in 2004 in its allograft products. Further, the Company relies on one supplier for its GRAFTJACKET® family of soft tissue repair and graft containment products, as well as one supplier for its ADCON® Gel products.

Income Taxes. Income taxes are accounted for pursuant to the provisions of SFAS No. 109, *"Accounting for Income Taxes"* ("SFAS No. 109"). The Company's effective tax rate is based on income by tax jurisdiction, statutory rates and tax saving initiatives available to it in the various jurisdictions in which it operates. Significant judgment is required in determining the Company's effective tax rate and evaluating its tax positions. This process includes assessing temporary differences resulting from differing recognition of items for income tax and accounting purposes. These differences result in deferred tax assets and liabilities, which are included within the Company's consolidated balance sheet.

Revenue Recognition. The Company's revenues are generated through two types of customers, hospitals and stocking distributors, with the majority of the Company's revenue derived from sales to hospitals. The Company's products are sold through a network of independent sales representatives in the U.S. and by a combination of employee sales representatives, independent sales representatives, and stocking distributors outside the U.S. Revenues from sales to hospitals are recorded when the hospital takes title to the product, which is when the product is surgically implanted in a patient and a purchase order is received from the hospital. The Company views the receipt of a purchase order as the evidence of customer acceptance of the product.

The Company records revenues from sales to its stocking distributors outside the U.S. at the time the product is shipped to the distributor. Stocking distributors, who sell the products to their customers, take title to the products and assume all risks of ownership. The Company's distributors are obligated to pay within specified terms regardless of when, if ever, they sell the products. In general, the distributors do not have any rights of return or exchange; however, in limited situations the Company has repurchase agreements with certain stocking distributors. Those certain agreements require the Company to repurchase a specified percentage of the inventory purchased by the distributor within a specified period of time prior to the expiration of the contract. During those specified periods, the Company defers the applicable percentage of the sales. Approximately $87,000 and $247,000 of deferred revenue related to these types of agreements was recorded at December 31, 2004 and 2003, respectively.

The Company must make estimates of potential future product returns related to current period product revenue. The Company develops these estimates by analyzing historical experience related to product returns. Judgment must be used and estimates made in connection with establishing the allowance for sales returns in any accounting period. An allowance for sales returns of $395,000 and $412,000 is included as a reduction of accounts receivable at December 31, 2004 and 2003, respectively.

Shipping and Handling Costs. The Company incurs shipping and handling costs associated with the shipment of goods to customers, independent distributors and its subsidiaries. All shipping and handling amounts billed to customers are included in net sales. All shipping and handling costs associated with the shipment of goods to customers are included in cost of

sales. All other shipping and handling costs are included in selling, general and administrative expenses.

Research and Development Costs. Research and development costs are charged to expense as incurred.

Foreign Currency Translation. The financial statements of the Company's international subsidiaries are translated into U.S. dollars using the exchange rate at the balance sheet date for assets and liabilities and the weighted average exchange rate for the applicable period for revenues, expenses, gains and losses. Translation adjustments are recorded as a separate component of comprehensive income. Gains and losses resulting from transactions denominated in a currency other than the local functional currency are included in other income.

Comprehensive Income. Comprehensive income is defined as the change in equity during a period related to transactions and other events and circumstances from non-owner sources. It includes all changes in equity during a period except those resulting from investments by owners and distributions to owners. The difference between the Company's net income and its comprehensive income is wholly attributable to foreign currency translation.

Stock-Based Compensation. At December 31, 2004, the Company has two stock-based employee compensation plans, which are described in Note 13. The Company accounts for those plans under the intrinsic value method in accordance with the provisions of Accounting Principles Board (APB) Opinion No. 25, "Accounting for Stock Issued to Employees." Accordingly, compensation cost related to stock option grants to employees has been recognized only to the extent that the fair market value of the stock exceeds the exercise price of the stock option at the date of the grant. Nonemployee stock-based compensation is accounted for in accordance with SFAS No. 123.

The following table illustrates the effect on net income and earnings per share if the Company had applied the fair value recognition provisions of SFAS No. 123, "Accounting for Stock-Based Compensation," to stock-based employee compensation (in thousands, except per share amounts):

Year Ended December 31,	2004	2003	2002
Net income, as reported	$24,022	$17,397	$25,060
Add: Stock-based employee compensation cost recognized under intrinsic value method, net of tax effects	681	920	998
Less: Stock-based employee compensation expense determined under fair value based method, net of tax effects	(8,626)	(4,334)	(2,918)
Pro forma net income	$16,077	$13,983	$23,140
Net income per share:			
Basic, as reported	$0.72	$0.53	$0.79
Basic, pro forma	$0.48	$0.43	$0.73
Diluted, as reported	$0.68	$0.50	$0.75
Diluted, pro forma	$0.47	$0.41	$0.69

In December 2004, the Financial Accounting Standards Board ("FASB") issued SFAS No. 123 (Revised 2004), "Share Based Payment," ("SFAS No. 123R"), effective for interim or annual reporting periods beginning after June 15, 2005. SFAS No. 123R requires the recognition of compensation expense for the fair value of share-based transactions. The fair value must be determined as of the date of grant using a valuation model such as Black-Scholes or a binomial lattice model. The Company has begun the process to evaluate and select an appropriate model for the valuation of its stock options. Until this evaluation is complete, the exact amount of the impact of SFAS No. 123R cannot be determined. The effect of expensing the fair value of the Company's stock options using the Black-Scholes model is presented in the table above.

Fair Value of Financial Instruments. The carrying value of cash and cash equivalents, accounts receivable, accounts payable and notes payable approximates the fair value of these financial instruments at December 31, 2004 and 2003 due to their short maturities or variable rates.

Derivative Instruments and Hedging Activities. The Company accounts for derivative instruments and hedging activities under SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities," as amended by SFAS No. 138. Accordingly, all of the Company's derivative instruments are recorded on the balance sheet as either an asset or liability and measured at fair value. The changes in the derivative's fair value are recognized currently in earnings unless specific hedge accounting criteria are met.

During the second half of 2004, the Company began a derivative program using 30-day foreign currency forward contracts to mitigate the risk of currency fluctuations on its intercompany receivable and payable balances that are denominated in foreign currencies. These forward contracts are expected to offset the transactional gains and losses on the related intercompany balances. These forward contracts are not designated as hedging instruments under SFAS No. 133. Accordingly, the changes in the fair value and the settlement of the contracts are recognized in the period incurred in the accompanying consolidated statement of operations.

For the year ended December 31, 2004, the Company recorded approximately $790,000 in losses on foreign currency contracts, which are included in "Other

income, net" in the Company's consolidated statement of operations. These losses offset translation gains recorded on the Company's intercompany receivable and payable balances. At December 31, 2004 and 2003, the Company did not have any outstanding foreign currency contracts.

Supplemental Cash Flow Information. Cash paid for interest expense and income taxes was as follows (in thousands):

Year Ended December 31,	2004	2003	2002
Interest	$ 717	$ 994	$ 883
Income taxes	$ 8,289	$ 4,411	$ 359

During 2004, the Company favorably resolved certain income tax contingencies associated with the Company's acquisition of Cremascoli, resulting in a decrease in goodwill of approximately $3.0 million. See Note 6 for further discussion of this matter. Additionally, the Company entered into capital leases of approximately $1.1 million and $628,000 during 2004 and 2003, respectively.

Reclassifications. Certain prior year amounts have been reclassified to conform to the 2004 presentation.

Recent Pronouncements. In November 2004, the FASB issued SFAS No. 151, *Inventory Costs - An Amendment of ARB No. 43, Chapter 4* ("SFAS No. 151"). SFAS No. 151 will no longer allow companies to capitalize inventory costs on their balance sheet when the production defect rate varies significantly from the expected rate. All abnormal freight, handling and material waste will be treated as period expenses. Additionally, SFAS No. 151 requires that a facility's fixed production overhead be charged to inventory based on a range of "normal" capacity. If the production level is abnormally low or high, unallocated overhead should be charged to current period expense. SFAS No. 151 is required to be adopted for annual periods beginning after June 15, 2005. Accordingly, the Company will adopt the provisions of SFAS No. 151 effective January 1, 2006. Management is evaluating the impact of this standard on its results of operations and financial statements.

In December 2004, the FASB issued two FASB Staff Positions ("FSP") in response to the American Jobs Creation Act of 2004 (the "Jobs Creation Act") related to accounting and disclosures associated with certain provisions of the Jobs Creation Act. (The Jobs Creation Act and management's evaluation of its impact is further described within the "Results of Operations" section of Item 7 of this report.) FSP 109-1 requires the deduction for qualified domestic production activities to be accounted for as a special deduction under SFAS No. 109, not as a tax-rate deduction. The Company will comply with the provisions of FSP 109-1 effective January 1, 2005, should this deduction become available to the Company. FSP 109-2 allows for additional time for companies to determine whether any foreign earnings will be repatriated under the Jobs Creation Act's one-time deduction for repatriated earnings. Companies that take the additional time are required to provide disclosures about the status of their evaluation. Based on management's assessment of the repatriation deduction, the Company has determined to continue its current policy of permanently reinvesting all foreign earnings and therefore, the provisions of FSP 109-2 are not applicable to the Company.

3. Acquisition of Assets:

On March 5, 2003, the Company completed an acquisition of certain assets from Gliatech Inc. related to its ADCON® Gel technology for $8.4 million in cash. Additionally, the Company entered into a royalty agreement that requires the Company to pay a royalty on future product sales. The Company paid $840,000 of the purchase price as a deposit in the fourth quarter of 2002, and $3.4 million in the first quarter of 2003. The remaining $4.2 million was paid in the second quarter of 2003 upon final receipt of all assets.

The following table summarizes the allocation of the purchase price (in thousands):

Inventories	$1,312
Property, plant and equipment	160
Acquired in-process research and development	4,558
Intangible assets:	
Completed Technology	1,575
Trademarks	554
Other	286
	$8,445

In connection with the acquisition of these assets, the Company engaged an independent third party to conduct a valuation of the intangible assets acquired. The value assigned to acquired in-process research and development ("IPRD") was $4.6 million of the purchase price. Accordingly, this amount was expensed in the first quarter of 2003. The value assigned to IPRD was determined by estimating the costs to develop the IPRD into commercially viable products, estimating the resulting cash flows from such projects, and discounting the net cash flows using a 32% risk adjusted discount rate. This discount rate reflected uncertainties surrounding the successful development of the IPRD.

4. Inventories:

Inventories consist of the following (in thousands):

December 31,	2004	2003
Raw materials	$3,373	$2,816
Work-in-process	14,306	9,827
Finished goods	58,590	51,561
	$76,269	$64,204

5. Property, Plant and Equipment:

Property, plant and equipment consists of the following (in thousands):

December 31,	2004	2003
Land and land improvements	$1,944	$1,567
Buildings	8,773	7,249
Machinery and equipment	31,849	26,922
Furniture, fixtures and office equipment	25,444	20,887
Construction in progress	2,284	5,654
Surgical instruments	56,963	45,664
	127,257	107,943
Less: Accumulated depreciation	(57,050)	(41,028)
	$70,207	$66,915

The components of property, plant and equipment recorded under capital leases consist of the following (in thousands):

December 31,	2004	2003
Land and land improvements	$269	$249
Buildings	3,247	3,116
Machinery and equipment	8,103	6,826
Furniture, fixtures and office equipment	2,135	1,873
	13,754	12,064
Less: Accumulated depreciation	(5,940)	(4,117)
	$7,814	$7,947

Depreciation expense approximated $17.3 million, $13.9 million, and $13.6 million for the years ended December 31, 2004, 2003, and 2002, respectively, and included amortization of assets under capital leases.

6. Goodwill and Intangible Assets:

Changes in the carrying amount of goodwill occurring during the year ended December 31, 2004 are as follows (in thousands):

Goodwill, at December 31, 2003	$11,248
Less: Resolution of pre-acquisition foreign income tax contingencies	(2,978)
Foreign currency translation	575
Goodwill, at December 31, 2004	$8,845

During 2004, the Company favorably resolved certain foreign income tax contingencies associated with its December 1999 acquisition of Cremascoli. These amounts were established as an accrued liability in the purchase accounting associated with the acquisition of Cremascoli. Due to the favorable resolution of these matters, the Company reduced the previously recorded goodwill and associated accrued liabilities, which were recorded in "Other liabilities" in the Company's consolidated balance sheet.

The components of the Company's identifiable intangible assets are as follows (in thousands):

	December 31, 2004		December 31, 2003	
	Cost	Accumulated Amortization	Cost	Accumulated Amortization
Distribution channels	$20,797	$10,399	$19,296	$7,708
Completed technology	5,348	1,733	5,288	1,025
Licenses	2,683	1,538	2,593	983
Trademarks	657	152	657	75
Other	3,303	1,826	1,752	1,149
	32,788	$15,648	29,586	$10,940
Less: Accumulated amortization	(15,648)		(10,940)	
Intangible assets, net	$17,140		$18,646	

Based on the intangible assets held at December 31, 2004, we expect to amortize approximately $4.0 million in 2005, $3.5 million in 2006, $2.9 million in 2007, $2.7 million in 2008 and $2.5 million in 2009.

7. Accrued Expenses and Other Current Liabilities:

Accrued expenses and other current liabilities consist of the following (in thousands):

December 31,	2004	2003
Employee benefits	$11,813	$11,480
Advances from factoring arrangement	5,242	4,780
Royalties	4,664	5,658
Taxes other than income	4,120	3,281
Commissions	3,818	3,423
Professional fees	3,129	2,333
Purchased technology	1,500	1,500
Legal	1,153	1,343
Other	9,817	9,016
	$45,256	$42,814

8. Earnings Per Share:

SFAS No. 128, "Earnings Per Share," requires the presentation of basic and diluted earnings per share. Basic earnings per share is calculated based on the weighted-average shares of common stock outstanding during the period. Diluted earnings per share is calculated to include any dilutive effect of the Company's common stock equivalents, which consist of stock options and warrants. The dilutive effect of such instruments is calculated using the treasury-stock method.

The weighted-average number of common shares outstanding for basic and diluted earnings per share purposes is as follows (in thousands):

Year Ended December 31,	2004	2003	2002
Weighted-average number of common shares outstanding - basic	33,391	32,857	31,870
Common stock equivalents	1,926	1,704	1,680
Weighted-average number of common shares outstanding - diluted	35,317	34,561	33,550

For the years ended December 31, 2004, 2003 and 2002, options to purchase approximately 1.7 million, 671,000 and 447,000, respectively, shares of the Company's common stock were excluded from the calculation of diluted earnings per share because the effect was antidilutive. These stock options were antidilutive because the exercise price of the options was greater than the average market price of common stock for the respective period.

9. Long-Term Obligations:

Long-term obligations consist of the following (in thousands):

December 31,	2004	2003
Notes payable	$8,750	$13,250
Capital lease obligations	3,533	4,074
	12,283	17,324
Less: current portion	(6,331)	(6,228)
	$5,952	$11,096

In August 2001, the Company entered into a five-year senior credit facility with a syndicate of commercial banks. This senior credit facility consists of $20 million in term loans and a revolving loan facility of up to $60 million. The Company had borrowings outstanding under the term loans of $8.8 million and $13.3 million at December 31, 2004 and 2003, respectively.

Borrowings under the senior credit facility are guaranteed by all of the Company's subsidiaries and collateralized by all of the assets of Wright Medical Technology, Inc., the Company's wholly-owned subsidiary. The credit facility contains customary covenants including, among other things, restrictions on the ability to pay cash dividends, prepay debt, incur additional debt and sell assets. The credit facility also requires the Company to maintain certain financial covenants, including a specified consolidated leverage (or debt-to-equity) ratio and a specified consolidated fixed charge coverage ratio. In the event that the Company violates any covenants, it could be required to repay the remaining balance of the debt. Additionally, should the Company be required to repay the loan before its scheduled maturity, a charge to operating income for unamortized financing costs would be incurred. At the Company's option, borrowings under the credit facility bear interest either at a rate equal to a fixed base rate plus a spread of 0.75% to 1.25% or at a rate equal to an adjusted LIBOR plus a spread of 1.75% to 2.25%, depending on the consolidated leverage ratio, with a current annual rate of 3.625%.

At December 31, 2004, the Company had availability under committed credit facilities, after considering outstanding letters of credit, totaling $59.7 million.

Aggregate annual maturities of the Company's long-term obligations at December 31, 2004, excluding capital lease obligations, are as follows (in thousands):

2005	$5,000
2006	3,750
	$8,750

As discussed in Note 5, the Company has acquired certain property and equipment pursuant to capital leases. These leases have various maturity dates ranging from one to six years with interest rates ranging from 2.81% to 10.14%. At December 31, 2004, future minimum lease payments under capital lease obligations, together with the present value of the net minimum lease payments, are as follows (in thousands):

2005	$1,642
2006	1,403
2007	790
2008	496
2009	368
Thereafter	333
Total minimum payments	5,032
Less amount representing interest	(1,499)
Present value of minimum lease payments	3,533
Current portion	(1,331)
Long-term portion	$2,202

10. Income Taxes:

The components of the Company's income before income taxes are as follows (in thousands):

Year Ended December 31,	2004	2003	2002
Domestic	$40,437	$25,675	$30,678
Foreign	(3,014)	1,444	(3,784)
Income before income taxes	$37,423	$27,119	$26,894

The components of the Company's provision for income taxes are as follows (in thousands):

Year Ended December 31,	2004	2003	2002
Current provision:			
Domestic:			
Federal	$12,815	$3,080	$ -
State	811	203	-
Foreign	4,401	1,404	819
Deferred provision (benefit):			
Domestic:			
Federal	(197)	4,313	1,331
State	803	1,098	1,841
Foreign	(5,232)	(376)	(2,157)
Total provision for income taxes	$13,401	$9,722	$1,834

A reconciliation of the statutory federal income tax rate to the Company's effective income tax rate is as follows:

Year Ended December 31,	2004	2003	2002
Income tax provision at statutory rate	35.0%	35.0%	35.0%
State tax provision	4.8%	4.4%	4.6%
Change in valuation allowance	(3.1%)	4.5%	(30.2%)
Meals and entertainment limitation	1.0%	1.2%	1.0%
Research and development credit	(2.6%)	(9.9%)	(1.4%)
Other, net	0.7%	0.7%	(2.2%)
Total	35.8%	35.9%	6.8%

The significant components of the Company's deferred tax assets and liabilities as of December 31, 2004 and 2003 are as follows (in thousands):

December 31,	2004	2003
Deferred tax assets:		
Operating loss carryforwards	$12,832	$18,367
General business credit carryforward	2,309	4,393
Alternative minimum tax credits	621	3,080
Reserves and allowances	19,399	14,219
Amortization	5,660	4,235
Other	11,718	10,180
Valuation allowance	(5,897)	(16,039)
Total deferred tax assets	46,642	38,435
Deferred tax liabilities:		
Depreciation	4,523	4,446
Acquired intangible assets	3,767	4,369
Other	5,570	2,015
Total deferred tax liabilities	13,860	10,830
Net deferred tax assets	$32,782	$27,605

Provisions for federal income taxes are not made on the undistributed earnings of foreign subsidiaries where the subsidiaries do not have the capability to remit earnings in the foreseeable future and when earnings are considered permanently invested. Deferred taxes are not provided for temporary differences related to earnings of non-U.S. subsidiaries that are intended to be permanently reinvested. At December 31, 2004, the Company did not have undistributed earnings of foreign subsidiaries, as total earnings from these subsidiaries have been offset by losses.

At December 31, 2004, the Company had net operating loss carryforwards for U.S. federal income tax purposes of approximately $16.7 million, which expire in 2017 and 2018. Additionally, the Company had general business credit carryforwards of approximately $2.3 million, which expire beginning in 2007 and extending through 2016, and alternative minimum tax credits of approximately $600,000, which do not expire. At December 31, 2004, the Company had foreign net operating loss carryforwards of approximately $20.2 million, of which $2.6 million expire beginning in 2004 and extending through 2010.

Certain of the Company's U.S. and foreign net operating losses and general business credit carryforwards are subject to various limitations. The Company maintains valuation allowances for these net operating losses and tax credit carryforwards that will expire unused due to these limitations.

During 2004, the Company completed certain tax studies. These studies indicated that a revision to the Company's original estimates of the limitations on the utilization of its net operating losses and tax credit carryforwards was required. Accordingly, the completion of the studies resulted in a reduction of approximately $10.7 million in the valuation allowance for these deferred tax assets as the deferred tax assets were more likely than not to be realized in the future. Additionally, these studies indicated that approximately $8.5 million of tax exposure exists as a result of the tax filing positions taken with respect to these net operating losses and tax credit carryforwards. Based on these findings, the Company reclassified approximately $8.5 million of the valuation allowance to its accruals for tax contingencies. The remaining reduction in the Company's valuation allowance was released through the income tax provision or was a result of currency fluctuations on the portion of its valuation allowances recorded in foreign currencies.

11. Other Long-Term Liabilities:

Other long-term liabilities consist of the following (in thousands):

December 31,	2004	2003
Accruals for tax contingencies	$12,951	$7,788
Other	604	429
	$13,555	$8,217

The Company establishes accruals for tax contingencies, when, despite its belief that tax return positions are fully supportable, certain of these positions may be challenged and the Company may not prevail upon review. During 2004, as discussed in Note 10, approximately $8.5 million of the Company's valuation allowance for deferred tax assets was reclassified to accruals for tax contingencies. Additionally, as discussed in Note 6, the Company favorably resolved certain foreign tax contingencies associated with its December 1999 acquisition of Cremascoli. The favorable resolution of these matters resulted in

a reduction of the Company's previously recorded accrual for tax contingencies and goodwill of approximately $3.0 million.

12. Capital Stock:

Common Stock. The Company is authorized to issue up to 100,000,000 shares of voting common stock. The Company has 66,149,798 shares of voting common stock available for future issuance at December 31, 2004.

Warrants. In connection with the December 1999 recapitalization, the Company issued warrants to stockholders and certain employees to purchase an aggregate of 727,276 shares of the Company's common stock at an exercise price of $4.35 per share. No warrants remain outstanding at December 31, 2004. The warrants were exercisable at any time after issuance and, unless exercised, expired five years from the date of issuance. During the years ended December 31, 2004, 2003 and 2002, warrants for 353,209, 6,691 and 349,194 shares were exercised, respectively.

13. Stock Option Plans:

At December 31, 2004, the Company has two stock-based incentive plans, which are described below. As permitted by SFAS No. 123, "Accounting for Stock-Based Compensation," the Company applies APB Opinion No. 25 and related interpretations in accounting for its employee stock option plans. Accordingly, compensation cost related to stock option grants to employees has been recognized only to the extent that the fair market value of the stock exceeds the exercise price of the stock option at the date of the grant.

Equity Incentive Plan

On December 7, 1999, the Company adopted the 1999 Equity Incentive Plan (the "Plan"), which was subsequently amended and restated on July 6, 2001, May 13, 2003 and May 13, 2004. The Plan authorizes the Company to grant options to purchase up to 8,267,051 shares of common stock. Under the Plan, options to purchase common stock generally are exercisable in increments of 25% annually in each of the first through fourth anniversaries of the date of grant. Options to purchase Series A Preferred Stock that were outstanding at the time the Company completed its IPO in July 2001 became options to purchase the Company's common stock. Those options were immediately exercisable upon their issuance. All the options issued under the plan expire after ten years.

The weighted-average fair value of the Company's options granted in 2004, 2003 and 2002 was $17.39 per share, $12.96 per share and $11.78 per share, respectively. The fair value of these options is estimated on the date of grant using the Black-Scholes methodology required by SFAS No. 123 for publicly traded companies. In applying the Black-Scholes methodology to the option grants, the Company used the following assumptions:

Year Ended December 31,	2004	2003	2002
Risk-free interest rate	4.0% - 4.8%	3.6% - 4.3%	4.0% - 5.0%
Expected option life	7 years	7 years	6 – 7 years
Expected price volatility	50.1%	54.3%	54.3%

The assumed forfeiture rate was not material to the calculation. The Company does not assume a dividend yield as it has never declared or paid cash dividends on its common stock.

A summary of the Company's stock option activity is as follows (shares in thousands):

	COMMON STOCK	
	Shares	Weighted Avg. Exercise Price
Outstanding at December 31, 2001	3,127	$5.09
Granted	630	18.09
Exercised	(374)	4.01
Forfeited or expired	(95)	9.30
Outstanding at December 31, 2002	3,288	$7.58
Granted	1,333	21.80
Exercised	(309)	4.67
Forfeited or expired	(78)	7.25
Outstanding at December 31, 2003	4,234	$12.28
Granted	2,458	30.61
Exercised	(505)	7.53
Forfeited or expired	(359)	24.34
Outstanding at December 31, 2004	5,828	$19.68

As of December 31, 2004, there were 1,014,744 options available for future issuance.

In 2004, 2003, and 2002, the Company granted certain independent distributors a total of 19,900, 16,750 and 15,850 common stock options, respectively, under the Plan. The distributors were given options to purchase common stock, exercisable in 25% increments on the first through fourth anniversaries of the date of grant, at a weighted-average exercise price of $32.56, $16.31 and $17.21 per share in 2004, 2003, and 2002, respectively. The options expire after ten years.

In connection with the distributor stock grants discussed above and the issuance of certain stock options to employees and distributors, the Company incurred stock-based compensation representing the fair value of the stock and stock options granted to distributors, and for employee stock options to the extent the fair value of the Company's stock exceeded the exercise price of the stock option at the date of the grant. The Company recognizes this stock-based compensation over the respective vesting period, as appropriate. For the years ended December 31, 2004, 2003 and 2002, stock-based expense of $1.5 million, $2.1 million, and $1.7 million, respectively, was recorded in the accompanying statement of operations related to these stock options and stock grants.

A summary of the Company's stock options outstanding and exercisable at December 31, 2004, is as follows (shares in thousands):

Options Outstanding				Options Exercisable	
Range of Exercise Prices	Number Outstanding	Weighted-Average Remaining Contractual Life	Weighted-Average Exercise Price	Number Exercisable	Weighted-Average Exercise Price
$0.00 – $8.50	1,872	5.5	$5.12	1,746	$4.95
$8.51 – $16.00	80	7.6	15.26	31	15.31
$16.01 – $24.00	1,125	8.0	18.26	340	18.09
$24.01 – $32.00	2,003	9.2	28.39	151	27.03
$32.01 – $35.87	748	9.5	35.36	-	-
	5,828	7.8	$19.68	2,268	$8.53

Employee Stock Purchase Plan

On May 30, 2002, the Company and its shareholders approved and adopted the 2002 Employee Stock Purchase Plan (the "ESPP"). The ESPP authorizes the Company to issue up to 200,000 shares of common stock to its employees who work at least 20 hours per week. Under the ESPP, there are two six-month plan periods during each calendar year, one beginning January 1 and ending on June 30, and the other beginning July 1 and ending on December 31. Under the terms of the ESPP, employees can choose each plan period to have up to 5% of their annual base earnings, limited to $5,000, withheld to purchase the Company's common stock. The purchase price of the stock is 85 percent of the lower of its beginning-of-period or end-of-period market price. Under the ESPP, the Company sold to employees 8,792, 12,777, and 5,682 shares in 2004, 2003, and 2002, respectively. The weighted-average fair value of those purchase rights granted in 2004, 2003, and 2002 was $9.04 per share, $5.27 per share, and $5.69 per share, respectively. As of December 31, 2004, there were 172,749 shares available for future issuance. In applying the Black-Scholes methodology to the purchase rights granted, the Company used the following assumptions:

Year Ended December 31,	2004	2003	2002
Risk-free interest rate	1.9% - 2.8%	1.1% - 1.8%	4.9%
Expected option life	6 months	6 months	6 months
Expected price volatility	50.1%	54.3%	54.3%

The assumed forfeiture rate was not material to the calculation. The Company does not assume a dividend yield as it has never declared or paid cash dividends on its common stock.

14. Employee Benefit Plans:

The Company sponsors a defined contribution plan under Section 401(k) of the Internal Revenue Code, which covers U.S. employees who are 21 years of age and over. Under this plan, the Company matches voluntary employee contributions at a rate of 100% for the first 2% of an employee's annual compensation and at a rate of 50% for the next 2% of an employee's annual compensation. Employees vest in the Company's contributions after three years of service with the Company. The Company's expense related to the plan was $831,000, $716,000, and $677,000 in 2004, 2003, and 2002, respectively.

15. Commitments and Contingencies:

Operating Leases. The Company leases certain equipment and office space under non-cancelable operating leases. Rental expense under operating leases approximated $6.2 million, $5.0 million and $3.9 million for the years ended December 31, 2004, 2003, and 2002, respectively. Future minimum payments, by year and in the aggregate, under non-cancelable operating leases with initial or remaining lease terms of one year or more, are as follows at December 31, 2004 (in thousands):

2005	$6,532
2006	4,626
2007	2,526
2008	556
2009	448
Thereafter	1,462
	$16,150

Royalty and Consulting Agreements. The Company has entered into various royalty and other consulting agreements with third party consultants. The Company incurred royalty and consulting expenses of $6.2 million, $5.0 million and $4.5 million during the years ended December 31, 2004, 2003, and 2002, respectively, under minimum contractual obligations that were contingent upon services. The amounts in the table below represent minimum payments to consultants that are contingent upon future services. These fees are accrued when it is deemed probable that the performance thresholds are met. Payments under these agreements for which the Company has not recorded a liability, are as follows at December 31, 2004 (in thousands):

2005	$6,266
2006	1,668
2007	1,235
2008	1,041
2009	957
Thereafter	4,000
	$15,167

Portions of the Company's payments for operating leases and royalty agreements are denominated in foreign currencies and were translated in the tables above based on their respective U.S. dollar exchange rates at December 31, 2004. These future payments are subject to foreign currency exchange rate risk.

Purchase Obligations. The Company has entered into certain supply agreements for its products, which include minimum purchase obligations. During the years ended December 31, 2004, 2003, and 2002, the Company paid approximately $6.4 million, $6.8 million, and $2.3 million, respectively, under those supply agreements. The amounts in the table below represent the Company's purchase obligations in future years under those supply agreements:

2005	$6,609
2006	5,263
	$11,872

Portions of these payments are denominated in foreign currencies and were translated based on their respective U.S. dollar exchange rates at December 31, 2004. These future payments are subject to foreign currency exchange rate risk.

Legal Proceedings. On June 30, 1993, prior to the December 1999 recapitalization and inception of the Company in its present form, the Predecessor Company acquired substantially all the assets of the large joint orthopaedic implant business from Dow Corning Corporation (DCC). DCC retains liability for matters arising from certain conduct of DCC prior to June 30, 1993. As such, DCC has agreed to indemnify the Predecessor Company against all liability for all products manufactured prior to the acquisition except for products provided under the Predecessor Company's 1993 agreement with DCC pursuant to which the Predecessor Company purchased certain small joint orthopaedic implants for worldwide distribution.

The Predecessor Company was notified in May 1995 that DCC, which filed for reorganization under Chapter 11 of the U.S. Bankruptcy Code, would no longer defend the Predecessor Company in such matters until it received further direction from the bankruptcy court. Based on the most recent plan of reorganization submitted to the court, it appears that the Predecessor Company would be considered an unsecured creditor and, under the terms of the plan, would receive 24% of any such claim as a cash payment with the remainder to be paid by a senior note due within ten years. There are several appeals regarding the confirmed plan of reorganization pending before the U.S. District Court in Detroit, Michigan, which have delayed implementation of the plan.

There can be no assurance that DCC will indemnify the Predecessor Company or the Company on any claims in the future. Although neither the Predecessor Company nor the Company maintains insurance for claims arising on products sold by DCC, the Company does not believe the outcome of any of these matters will have a material adverse effect on the Company's financial position or results of operations.

In 2000, Howmedica Osteonics Corp. ("Howmedica") filed a lawsuit against the Company alleging patent infringement. The lawsuit seeks an order of infringement, injunctive relief, unspecified damages and various other costs and relief. The claims in this case could impact a substantial portion of our knee product line. The Company believes, however, that it has strong defenses against the claims and that the claims are, in part, covered by the Company's patent infringement insurance. In 2004, a Markman hearing was held regarding interpretation of the patent claims that have been asserted by Howmedica in this lawsuit. The court has taken the issue of claim interpretation under advisement and both parties await the decision of the court on this issue. Management is unable to estimate the potential liability, if any, with respect to the claims and accordingly, no provision has been made for this contingency as of December 31, 2004. However, management does not believe that the outcome of this lawsuit will have a material adverse effect on the Company's financial position or results of operations.

In July 2002, the Company entered into a license agreement to resolve an intellectual property dispute that, among other things, provided for a payment of up to $1.25 million if a particular patent re-issued by February 10, 2004, and certain other conditions, as defined in the license agreement, were satisfied. While the patent in question re-issued prior to February 10, 2004, based on its assessment, the Company has concluded that the other required conditions were not satisfied upon re-issuance and the consequential payment of any amount is not probable. Accordingly, no provision has been made for this contingency as of December 31, 2004.

In July 2002, pursuant to a purchase and royalty agreement with CERAbio LLC ("CERAbio"), the Company purchased assets consisting primarily of completed technology for $3.0 million and recorded this entire amount as an intangible asset. Of this purchase price, $1.5 million was paid upon signing the purchase agreement. The remaining $1.5 million is recorded in "Accrued expenses and other current liabilities" in the consolidated balance sheet and is due once certain conditions under the agreement are satisfied. The agreement also provides for specified future royalties contingent upon sales of products related to the acquired technology. The Company, believing that the contractual obligations for payment had not been met, disputed whether the

second payment and royalties had been earned. In 2003, CERAbio and Phillips Plastics Corporation filed a lawsuit against the Company in United States District Court for the Western District of Wisconsin for payment of the remaining $1.5 million of the purchase price and the royalties earned to date. In November 2003, the trial court ruled in favor of CERAbio and ordered the Company to pay the remaining purchase price and the royalties earned to date. The royalties earned to date have been recorded within "Accrued expenses and other current liabilities" in the consolidated balance sheet. In 2004, the Company appealed the trial court's judgment to the United States Court of Appeals for the Seventh Circuit, briefs and oral arguments were submitted, and the appeal is pending. The Company does not believe that the outcome of this lawsuit will have a material adverse affect on its financial position or results of operations.

In September 2004, the Company announced a voluntary market withdrawal of a limited number of metal acetabular hip cups that are intended for use in the Company's CONSERVE® hip systems. In connection with this market withdrawal, the Company recorded $500,000 in product liability reserves for probable losses related to the market withdrawal. Management developed this estimate and believes that the amount recorded is appropriate based on assumptions with respect to estimated patient claims related to the market withdrawal and the acceptance of such claims by our insurer. The nature of a market withdrawal and the associated claims are such that the claims will occur over an extended period of time. The Company's loss estimate includes an assumption for unasserted claims based on management's industry experience with similar circumstances. While the Company believes that the amount recorded related to the market withdrawal is appropriate, it is possible that changes in assumptions related to potential claims or insurance coverage could have an adverse effect on the Company's estimate.

The Company is currently involved in separate disputes, in Italy, with a former agent and two former employees. No lawsuits have been filed by a party in any of these matters. Management believes that it has meritorious defenses should any claim arise and that the payment of any amount is not probable and cannot be estimated at this time. Accordingly, no provisions have been made for these matters as of December 31, 2004.

In addition to those noted above, the Company is subject to various other legal proceedings, product liability claims and other matters which arise in the ordinary course of business. In the opinion of management, the amount of liability, if any, with respect to these matters will not materially affect the results of operations or financial position of the Company.

16. Segment Data:

The Company has one reportable segment, orthopaedic products, which includes the design, manufacture and marketing of reconstructive joint devices and biologics products. The Company's geographic business units consist of operations in the United States, Europe and Other (which principally represents Canada and Japan). Identifiable assets are those assets used exclusively in the operations of each business unit. Revenues attributed to each geographic unit are based on the location in which the sale originated.

Net sales of orthopaedic products by category and information by geographic area are as follows (in thousands):

Year Ended December 31,	2004	2003	2002
Net sales by product line:			
Hips products	$99,133	$78,071	$56,945
Knee products	87,408	78,338	72,058
Biologics products	62,070	50,056	38,347
Extremity products	36,433	31,876	25,367
Other	12,495	10,591	8,156
Total	$297,539	$248,932	$200,873
Net sales by geographic business unit:			
United States	$200,500	$168,138	$138,853
Europe	74,292	61,075	47,011
Other	22,747	19,719	15,009
Total	$297,539	$248,932	$200,873
Operating income by geographic business unit:			
United States	$33,102	$19,472	$24,136
Europe	(433)	3,912	1,844
Other	5,744	3,782	575
Total	$38,413	$27,166	$26,555

December 31,	2004	2003
Long-lived assets:		
United States	$45,905	$44,863
Europe	18,012	18,688
Other	6,290	3,364
Total	$70,207	$66,915

Sales to United States-based customers, aggregated $180.4 million, $152.9 million, and $122.4 million, for the years ended December 31, 2004, 2003, and 2002, respectively. These sales, along with United States export sales, are included in United States sales in the above table. No single foreign country accounted for more than 10% of the Company's total net sales during 2004, 2003 or 2002; however, Italy and France together represented approximately 16% of the Company's total net sales in each of 2004, 2003 and 2002.

17. Quarterly Results of Operations (unaudited):

The following table presents a summary of the Company's unaudited quarterly operating results for each of the four quarters in 2004 and 2003, respectively (in thousands). This information was derived from unaudited interim financial statements that, in the opinion of management, have been prepared on a basis consistent with the financial statements contained elsewhere in this filing and include all adjustments, consisting only of normal recurring adjustments, necessary for a fair statement of such information when read in conjunction with our audited financial statements and related notes. The operating results for any quarter are not necessarily indicative of results for any future period.

	2004			
	Q1	Q2	Q3	Q4
Net sales	$74,917	$ 75,616	$ 69,299	$77,707
Cost of sales	20,386	21,383	19,998	22,416
Gross profit	54,531	54,233	49,301	55,291
Operating expenses:				
Selling, general and administrative	37,134	37,714	36,611	39,685
Research and development	4,982	4,524	4,302	4,613
Amortization of intangible assets	942	928	975	1,044
Stock-based expense	424	465	271	329
Total operating expenses	43,482	43,631	42,159	45,671
Operating income	$ 11,049	$ 10,602	$ 7,142	$ 9,620

	2003			
	Q1	Q2	Q3	Q4
Net sales	$58,622	$ 62,152	$ 59,268	$ 68,890
Cost of sales	15,540	17,386	15,453	19,436
Gross profit	43,082	44,766	43,815	49,454
Operating expenses:				
Selling, general and administrative	30,305	31,963	32,292	33,052
Research and development	3,535	3,908	4,397	4,311
Amortization of intangible assets	804	923	900	935
Stock-based expense	409	420	482	757
Acquired in-process R&D costs	4,558	-	-	-
Total operating expenses	39,611	37,214	38,071	39,055
Operating income	$ 3,471	$ 7,552	$ 5,744	$ 10,399

Report of Independent Registered Public Accounting Firm

The Board of Directors and Stockholders
Wright Medical Group, Inc.:

We have audited the accompanying consolidated balance sheets of Wright Medical Group, Inc. and subsidiaries as of December 31, 2004 and 2003, and the related consolidated statements of operations, changes in stockholders' equity and comprehensive income, and cash flows for each of the years in the three-year period ended December 31, 2004. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Wright Medical Group, Inc. and subsidiaries as of December 31, 2004 and 2003, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 2004, in conformity with U.S. generally accepted accounting principles.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of the internal control over financial reporting of Wright Medical Group, Inc. and subsidiaries as of December 31, 2004, based on criteria established in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), and our report dated February 21, 2005 expressed an unqualified opinion on management's assessment of, and the effective operation of, internal control over financial reporting.

KPMG LLP

Memphis, Tennessee
February 21, 2005

Report of Independent Registered Public Accounting Firm

The Board of Directors and Stockholders
Wright Medical Group, Inc.:

We have audited management's assessment, included in the accompanying Management's Annual Report on Internal Control Over Financial Reporting, that Wright Medical Group, Inc. and subsidiaries maintained effective internal control over financial reporting as of December 31, 2004, based on criteria established in *Internal Control—Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express an opinion on management's assessment and an opinion on the effectiveness of the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, evaluating management's assessment, testing and evaluating the design and operating effectiveness of internal control, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, management's assessment that Wright Medical Group, Inc. and subsidiaries maintained effective internal control over financial reporting as of December 31, 2004, is fairly stated, in all material respects, based on criteria established in *Internal Control—Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Also, in our opinion, Wright Medical Group, Inc. and subsidiaries maintained, in all material respects, effective internal control over financial reporting as of December 31, 2004, based on criteria established in *Internal Control—Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of Wright Medical Group, Inc. and subsidiaries as of December 31, 2004 and 2003, and the related consolidated statements of operations, changes in stockholders' equity and comprehensive income, and cash flows for each of the years in the three-year period ended December 31, 2004, and our report dated February 21, 2005 expressed an unqualified opinion on those consolidated financial statements.

KPMG LLP

Memphis, Tennessee
February 21, 2005

Management's Annual Report on Internal Control Over Financial Reporting

Our management is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Rule 13a-15(f) under the Securities Exchange Act of 1934. Under the supervision and with the participation of our management, including our principal executive officer and principal financial officer, we conducted an evaluation of the effectiveness of our internal control over financial reporting as of December 31, 2004, based on the criteria established in *Internal Control – Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Based on this evaluation, our management concluded that our internal control over financial reporting was effective as of December 31, 2004. Our management's assessment of the effectiveness of our internal control over financial reporting as of December 31, 2004, has been audited by KPMG LLP, an independent registered public accounting firm, as stated in their report which is included herein.

corporate information

Investor Relations

Stockholders, securities analysts and investors seeking more information can access the following information via the Internet at www.wmt.com:

- News releases describing significant Company events and sales and earnings results for each quarter and the fiscal year.
- Annual, Quarterly, and Current Reports to the Securities and Exchange Commission describing the Company's business and financial condition.

In addition, investors are welcome to call, write or fax Wright to request the information above – including a copy of the Company's Annual Report 10K, free of charge. Inquiries should be directed to:

Wright Medical Group, Inc.
Attn: Investor Relations
5677 Airline Road, Arlington, TN 38002
901.867.4113 901.867.4390 Fax

Transfer Agent and Registrar

American Stock Transfer & Trust Company, Inc. acts as transfer agent and registrar for Wright and maintains all stockholder records for the Company. Communications concerning stock holdings, lost certificates, transfer of shares, duplicate mailings or changes of address should be directed to:

Wright Medical Group, Inc.
c/o American Stock Transfer & Trust Company
59 Maiden Lane, New York, NY 10038
800.937.5449 info@amstock.com

Cash Dividend Policy

Wright has never declared or paid cash dividends on common stock and does not anticipate a change in this policy in the foreseeable future. The Company currently intends to retain any future earnings to fund the operation and expansion of its business.

Stock Prices and Trading Data

The Company's common stock is traded on the Nasdaq National Market under the symbol "WMGI". Stock price quotations are available at the Company's investor relations website at www.wmt.com, and are printed daily in major newspapers including The Wall Street Journal.

The ranges of high and low bid prices per share for the Company's Common Stock for 2004 and 2003 are set forth below. Price data reflect actual transactions. In all cases, the prices shown are inter-dealer prices and do not reflect markups, markdowns or commissions.

2004	High*	Low*	**2003**	High*	Low*
First Quarter	$35.53	$29.24		$17.85	$14.02
Second Quarter	$36.99	$29.56		$21.77	$16.24
Third Quarter	$36.08	$22.90		$26.75	$18.80
Fourth Quarter	$30.10	$20.75		$30.51	$24.50

* denotes high & low bid prices

Annual Meeting

The 2005 annual meeting of Wright stockholders will be held Thursday, May 12, 2005 beginning at 3:30pm CST at the Doubletree Hotel, Executive Meeting Room 5069 Sanderlin Avenue, Memphis, TN 38117

The Notice of Annual Meeting and Proxy Statement are being mailed to shareholders with this annual report.

Independent Auditors

KPMG LLP
Memphis, Tennessee

Non-GAAP Financial Measures

The Company uses non-GAAP financial measures, such as net sales, excluding the impact of foreign currency, gross profit, as adjusted, operating income, as adjusted, net income, as adjusted and net income, as adjusted, per diluted share. The Company's management believes that the presentation of these measures provides useful information to investors. These measures may assist investors in evaluating the Company's operations, period over period. The measures exclude such items as business development activities, including purchased in-process research and development, and the financial impact of significant litigation, which may be highly variable, difficult to predict and of a size that could have substantial impact on the Company's reported results of operations for a period. Management uses these measures internally for evaluation of the performance of the business, including the allocation of resources and the evaluation of results relative to employee performance compensation targets. Investors should consider these non-GAAP measures only as a supplement to, not as a substitute for or as superior to, measures of financial performance prepared in accordance with GAAP. This annual report includes discussion of non-GAAP financial measures. Reference is made to the most directly comparable GAAP financial measures, the reconciliation of the differences between the two financial measures is found on page 1 of this annual report, is otherwise available in the "Corporate - Investor Information - Supplemental Financial Information" section of the Company's website located at www.wmt.com.

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