# STRYKER CORP (SYK)

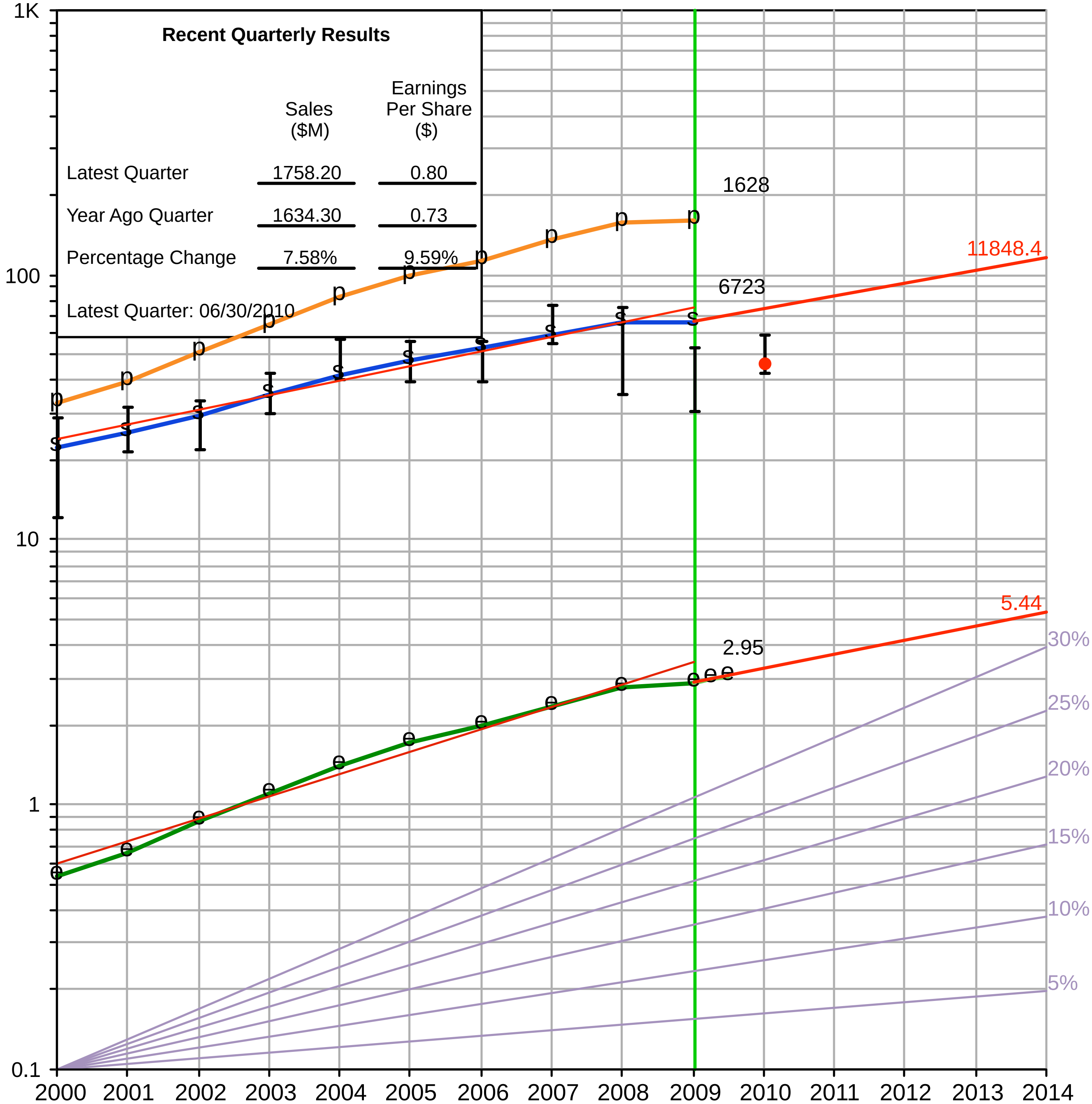
Date: 9/12/2010

**Stock Prices**
Current Price = $46.67
Exchange: NYSE
Industry:

52 Week Range = $42.74 to $59.72

Debt ($M): 1015.20
% Total Cap.: 13.08%

| **Share Data** | Authorized | Issued | |
|---|---|---|---|
| Preferred: | | 0.000 | |
| Common: | 399.200 | 396.900 | |
| Preferred Stock Dividend: | | | Dilution: 2.300 |




**Recent Quarterly Results**

| | Sales ($M) | Earnings Per Share ($) |
|---|---|---|
| Latest Quarter | 1758.20 | 0.80 |
| Year Ago Quarter | 1634.30 | 0.73 |
| Percentage Change | 7.58% | 9.59% |

Latest Quarter: 06/30/2010

(1) Historical Sales Growth = 13.65%
(2) Estimated Sales Growth = 12.00%

(3) Historical EPS Growth = 21.54%
(4) Estimated EPS Growth = 13.0%

ACE 5-year EPS Growth Estimate: 13.0%

## 2 EVALUATING MANAGEMENT



| | 2000 | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 | 2007 | 2008 | 2009 | 5 Yr Ave | Trend |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| % Pretax Profit on Sales (Net Before Tax/Sales) | 14.6 | 15.6 | 17.4 | 18.2 | 19.7 | 20.9 | 21.4 | 23.2 | 24.0 | 24.2 | 22.7 | UP |
| % Earned on Invested Capital (EPS/Book Val) | 25.2 | 24.9 | 23.3 | 20.8 | 20.9 | 21.8 | 19.6 | 18.3 | 20.7 | 17.8 | 19.6 | DOWN |
| % Debt to Equity | 102.6 | 68.1 | 32.8 | 0.9 | 0.0 | 5.7 | 0.0 | 0.0 | 0.0 | 0.0 | 1.1 | DOWN |

## 3 PRICE & EARNINGS HISTORY

Current Price: 46.67 52 Week High= 59.72 52 Week Low= 42.74

| Year | High Price | Low Price | EPS | PE High | PE Low | Dividend | Payout | High Yield |
|---|---|---|---|---|---|---|---|---|
| 2005 | 56.3 | 39.7 | 1.75 | 32.2 | 22.7 | 0.110 | 6.3 | 0.3 |
| 2006 | 55.9 | 39.8 | 2.02 | 27.7 | 19.7 | 0.220 | 10.9 | 0.6 |
| 2007 | 76.9 | 54.9 | 2.40 | 32.0 | 22.9 | 0.330 | 13.8 | 0.6 |
| 2008 | 74.9 | 35.4 | 2.83 | 26.5 | 12.5 | 0.400 | 14.1 | 1.1 |
| 2009 | 52.7 | 30.8 | 2.95 | 17.9 | 10.4 | 0.250 | 8.5 | 0.8 |
| TOTAL | 316.7 | 200.6 | | | | | | |
| AVE | 63.3 | 40.1 | | 27.3 | 17.6 | | 10.7 | |
| Average Price Earnings Ratio: 22.5 | | | | | Current Price Earnings Ratio: 15.0 | | | |

Current PE Ratio Based on Current EPS [$3.11]
Projected PE Ratio of [13.3] Based on Projected EPS [$3.5]

## 4 EVALUATING BUY, HOLD, & SELL

### A. CALCULATED HIGH PRICE - 5 YEARS

Ave High PE _21.0_ X Estimated High Earnings/Share _5.44_ Projected High Price = $_114.2_

### B. CALCULATED LOW PRICE - 5 YEARS

(a) Avg. Low P/E _17.6_ X Estimated Low Earnings/Share _2.95_ = $_51.92_
(b) Avg. Low Price of Last 5 Years = $40.1 (e) Price Variant = $37.8
(c) Recent Market Low = $30.8
(d) Dividend Price Support = $22.7

Selected Estimated Low Price $_37.8_

### C. BUY/HOLD/SELL ZONES

Selected High of $114.20 minus Selected Low of $37.80 = $76.40 Range. 1/4 of Range = $19.100

**25%/50%/25% Zoning**

Lower 1/3 = _$37.8_ To _$56.90_ (Buy)
Center 1/3 = _$56.90_ To _$95.10_ (Hold)
Upper 1/3 = _$95.10_ To _$114.2_ (Sell)

### D. UPSIDE RISK ANALYSIS

$$\frac{\text{High Price } 114.2 - \text{Current Price } 46.67}{\text{Current Price } 46.67 - \text{Low Price } 37.8} = 7.6 \text{ to } 1$$

**Current price of $46.67 is in the BUY zone**

PEG Ratio = 1.15 Relative Value = 66.7%
Proj PEG = 1.02 Proj Rel Value = 59.0%

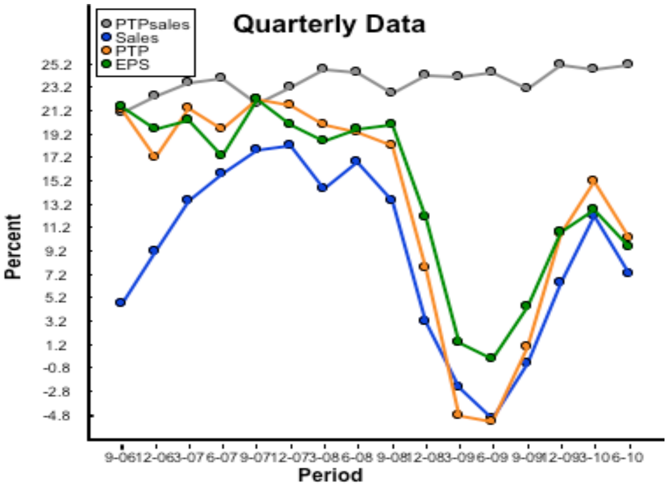
## 5 YIELD ANALYSIS

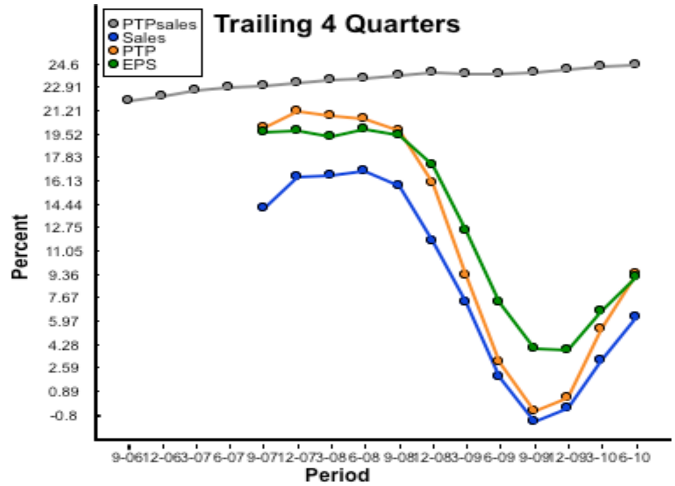
Current Yield = (100 * Current Dividend)÷Current Price = 100 * 0.60 / 46.7 = 1.3%
Ave. 5 Yr. Yield = (Ave. EPS(5Yr) * Ave. Payout)÷Current Price = (4.26 * 10.7)/46.7 = 1.0%

Price Appreciation = ((100*Projected High Price÷Current Price)-100)÷5 = 28.9 %
Average Total Return = Price Appreciation+Ave. 5 Yr. Yield = 29.9 %

| | P.A.R | Tot. Ret. |
|---|---|---|
| Average Yield | 0.6% | 0.5% |
| Annual Appreciation | 17.6% | 19.6% |
| Compounded Annual Return | 18.2% | 20.1% |

**Company: STRYKER CORP** **Symbol: SYK**




**Quarterly Performance** **Trailing Twelve Months**

## Quarterly Performance

| Period | SALES $ mil | SALES % Chg | PRETAX PROFIT $ mil | PRETAX PROFIT % Sales | PRETAX PROFIT % Chg | EARNINGS $ | EARNINGS % Chg |
|---|---|---|---|---|---|---|---|
| 6-10 | 1758.2 | 7.6% | 442.6 | 25.2% | 10.6% | 0.80 | 9.6% |
| 3-10 | 1799.1 | 12.4% | 445.8 | 24.8% | 15.4% | 0.80 | 12.7% |
| 12-09 | 1834.2 | 6.8% | 460.6 | 25.1% | 11.0% | 0.82 | 10.8% |
| 9-09 | 1653.3 | 0.0% | 381.4 | 23.1% | 1.4% | 0.69 | 4.5% |
| 6-09 | 1634.3 | -4.6% | 400.0 | 24.5% | -4.8% | 0.73 | 0.0% |
| 3-09 | 1601.3 | -2.0% | 386.4 | 24.1% | -4.4% | 0.71 | 1.4% |
| 12-08 | 1718.2 | 3.6% | 415.0 | 24.2% | 8.1% | 0.74 | 12.1% |
| 9-08 | 1653.0 | 13.7% | 376.0 | 22.7% | 18.3% | 0.66 | 20.0% |
| 6-08 | 1712.6 | 17.0% | 420.1 | 24.5% | 19.5% | 0.73 | 19.7% |
| 3-08 | 1634.4 | 14.7% | 404.0 | 24.7% | 20.1% | 0.70 | 18.6% |
| 12-07 | 1658.1 | 18.4% | 384.0 | 23.2% | 21.7% | 0.66 | 20.0% |
| 9-07 | 1453.2 | 18.0% | 317.9 | 21.9% | 22.2% | 0.55 | 22.2% |
| 6-07 | 1463.7 | 16.0% | 351.6 | 24.0% | 19.7% | 0.61 | 17.3% |
| 3-07 | 1425.5 | 13.7% | 336.4 | 23.6% | 21.5% | 0.59 | 20.4% |
| 12-06 | 1400.4 | 9.5% | 315.6 | 22.5% | 17.3% | 0.55 | 19.6% |
| 9-06 | 1231.1 | 5.1% | 260.2 | 21.1% | 21.4% | 0.45 | 21.6% |

## Trailing Twelve Months

| Period | SALES $ mil | PRETAX PROFIT $ mil | PRETAX PROFIT % Sales | EPS $ | PERCENT CHANGE Sales | PERCENT CHANGE PTP | PERCENT CHANGE EPS |
|---|---|---|---|---|---|---|---|
| 6-10 | 7044.8 | 1730.4 | 24.6% | 3.11 | 6.6% | 9.7% | 9.5% |
| 3-10 | 6920.9 | 1687.8 | 24.4% | 3.04 | 3.5% | 5.7% | 7.0% |
| 12-09 | 6723.1 | 1628.4 | 24.2% | 2.95 | 0.1% | 0.8% | 4.2% |
| 9-09 | 6607.1 | 1582.8 | 24.0% | 2.87 | -0.8% | -0.1% | 4.4% |
| 6-09 | 6606.8 | 1577.4 | 23.9% | 2.84 | 2.3% | 3.4% | 7.6% |
| 3-09 | 6685.1 | 1597.5 | 23.9% | 2.84 | 7.7% | 9.6% | 12.7% |
| 12-08 | 6718.2 | 1615.1 | 24.0% | 2.83 | 12.0% | 16.2% | 17.4% |
| 9-08 | 6658.1 | 1584.1 | 23.8% | 2.75 | 15.9% | 19.9% | 19.6% |
| 6-08 | 6458.3 | 1526.0 | 23.6% | 2.64 | 17.0% | 20.7% | 20.0% |
| 3-08 | 6209.4 | 1457.5 | 23.5% | 2.52 | 16.7% | 20.9% | 19.4% |
| 12-07 | 6000.5 | 1389.9 | 23.2% | 2.41 | 16.6% | 21.2% | 19.9% |
| 9-07 | 5742.8 | 1321.5 | 23.0% | 2.30 | 14.3% | 20.1% | 19.8% |
| 6-07 | 5520.7 | 1263.8 | 22.9% | 2.20 | | | |
| 3-07 | 5318.8 | 1206.0 | 22.7% | 2.11 | | | |
| 12-06 | 5147.2 | 1146.5 | 22.3% | 2.01 | | | |
| 9-06 | 5025.3 | 1100.0 | 21.9% | 1.92 | | | |

# STRYKER CORP (SYK)

Date: 9/12/2010

**Stock Prices**
Current Price = $46.67
Exchange: NYSE
Industry:

52 Week Range = $42.74 to $59.72

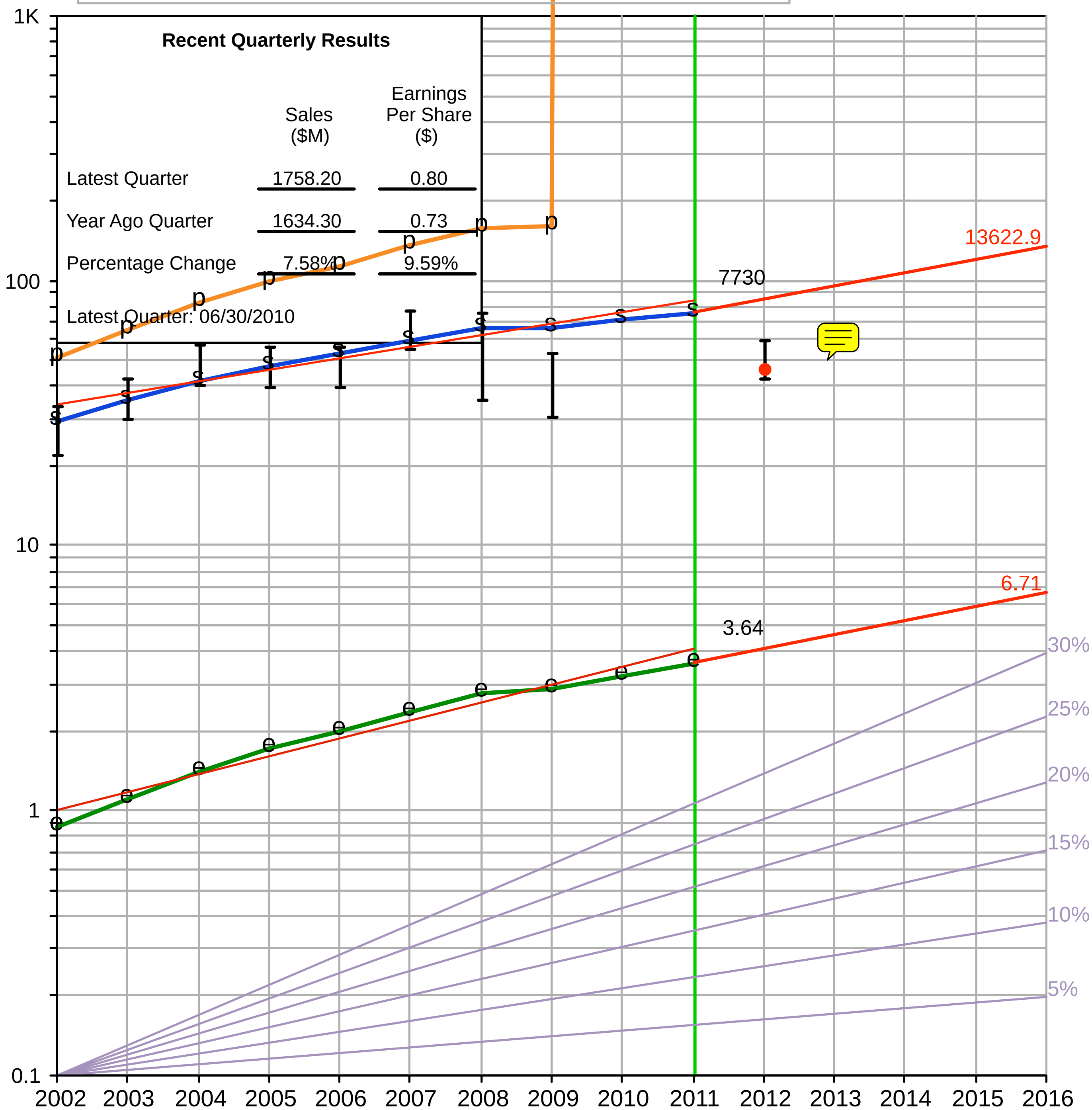
Debt ($M): 1015.20
% Total Cap.: 13.08%

| **Share Data** | Authorized | Issued | |
|---|---|---|---|
| Preferred: | | 0.000 | |
| Common: | 399.200 | 396.900 | |
| Preferred Stock Dividend: | | | Dilution: 2.300 |

**Recent Quarterly Results**

| | Sales ($M) | Earnings Per Share ($) |
|---|---|---|
| Latest Quarter | 1758.20 | 0.80 |
| Year Ago Quarter | 1634.30 | 0.73 |
| Percentage Change | 7.58% | 9.59% |

Latest Quarter: 06/30/2010




(1) Historical Sales Growth = 10.63%
(2) Estimated Sales Growth = 12.00%

(3) Historical EPS Growth = 16.71%
(4) Estimated EPS Growth = 13.0%

ACE 5-year EPS Growth Estimate: 13.0%

Printed: 9/12/2010 12:14 PM Prepared by: ETANA Using The Stock Investment Guide by Churr Software

# STRYKER CORP. NYSE-SYK

| RECENT PRICE | 46.69 | P/E RATIO | 14.1 (Trailing: 15.9; Median: 30.0) | RELATIVE P/E RATIO | 0.97 | DIV'D YLD | 1.3% | VALUE LINE |
|---|---|---|---|---|---|---|---|---|

TIMELINESS **2** Lowered 4/30/10
SAFETY **1** Raised 8/28/09
TECHNICAL **3** Lowered 3/5/10
BETA .80 (1.00 = Market)

| | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 | 2007 | 2008 | 2009 | 2010 | 2011 | 2012 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| High: | 18.3 | 28.9 | 31.6 | 33.7 | 42.7 | 57.7 | 56.3 | 55.9 | 76.9 | 74.9 | 52.7 | 59.7 |
| Low: | 11.1 | 12.2 | 21.7 | 21.9 | 29.8 | 40.3 | 39.7 | 39.8 | 54.9 | 35.4 | 30.8 | 45.5 |

Target Price Range 2013 | 2014 | 2015

**2013-15 PROJECTIONS**

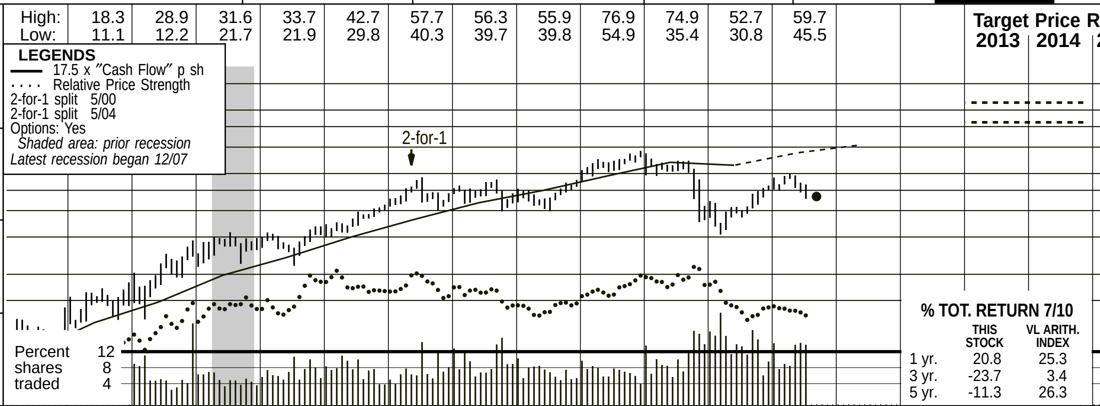
| | Price | Gain | Ann'l Total Return |
|---|---|---|---|
| High | 130 | (+180%) | 30% |
| Low | 105 | (+125%) | 23% |

**Insider Decisions**

| | O | N | D | J | F | M | A | M | J |
|---|---|---|---|---|---|---|---|---|---|
| to Buy | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Options | 0 | 1 | 0 | 2 | 3 | 3 | 1 | 0 | 0 |
| to Sell | 0 | 0 | 0 | 0 | 3 | 0 | 1 | 0 | 0 |

**Institutional Decisions**

| | 3Q2009 | 4Q2009 | 1Q2010 |
|---|---|---|---|
| to Buy | 339 | 302 | 298 |
| to Sell | 363 | 398 | 412 |
| Hld's(000) | 241787 | 239878 | 240569 |




**% TOT. RETURN 7/10**

| | THIS STOCK | VL ARITH. INDEX |
|---|---|---|
| 1 yr. | 20.8 | 25.3 |
| 3 yr. | -23.7 | 3.4 |
| 5 yr. | -11.3 | 26.3 |

| 1994 | 1995 | 1996 | 1997 | 1998 | 1999 | 2000 | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 | 2007 | 2008 | 2009 | 2010 | 2011 | © VALUE LINE PUB., INC. | 13-15 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| 1.76 | 2.24 | 2.35 | 2.55 | 2.86 | 5.41 | 5.84 | 6.61 | 7.60 | 9.08 | 10.59 | 12.02 | 13.25 | 14.60 | 16.95 | 16.90 | **18.40** | **19.90** | Sales per sh | **25.95** |
| .24 | .30 | .33 | .41 | .49 | .67 | .84 | 1.13 | 1.37 | 1.71 | 2.08 | 2.49 | 2.85 | 3.33 | 3.87 | 3.75 | **4.30** | **4.70** | "Cash Flow" per sh | **6.50** |
| .19 | .23 | .26 | .32 | .38 | .41 | .55 | .67 | .88 | 1.12 | 1.43 | 1.75 | 2.02 | 2.40 | 2.78 | 2.77 | **3.25** | **3.65** | Earnings per sh A | **5.35** |
| .01 | .01 | .03 | .03 | .03 | .03 | .04 | .04 | .05 | .06 | .09 | .11 | .22 | .33 | .40 | .25 | **.60** | **.64** | Div'ds Decl'd per sh B | **.84** |
| .08 | .09 | .07 | .09 | .13 | .20 | .21 | .41 | .35 | .36 | .47 | .67 | .53 | .46 | .39 | .33 | **.40** | **.40** | Cap'l Spending per sh | **.40** |
| .93 | 1.17 | 1.37 | 1.59 | 1.69 | 1.73 | 2.18 | 2.68 | 3.78 | 5.40 | 6.84 | 8.03 | 10.27 | 13.09 | 13.64 | 16.57 | **18.75** | **21.30** | Book Value per sh C | **32.75** |
| 386.95 | 388.43 | 387.15 | 384.24 | 386.16 | 388.80 | 391.80 | 393.40 | 396.20 | 399.40 | 402.50 | 405.20 | 407.90 | 411.00 | 396.40 | 397.90 | **394.50** | **391.50** | Common Shs Outst'g D | **391.00** |
| 21.2 | 24.6 | 25.0 | 27.5 | 26.7 | 35.5 | 37.1 | 40.3 | 33.0 | 32.4 | 33.0 | 27.7 | 23.6 | 27.9 | 21.8 | 15.1 | *Bold figures are* | | Avg Ann'l P/E Ratio | **22.0** |
| 1.39 | 1.65 | 1.57 | 1.59 | 1.39 | 2.02 | 2.41 | 2.07 | 1.80 | 1.85 | 1.74 | 1.47 | 1.27 | 1.48 | 1.31 | 1.01 | *Value Line* | | Relative P/E Ratio | **1.45** |
| .3% | .2% | .4% | .3% | .3% | .2% | .2% | .1% | .2% | .2% | .2% | .2% | .5% | .5% | .7% | .6% | *estimates* | | Avg Ann'l Div'd Yield | **.7%** |

**CAPITAL STRUCTURE as of 6/30/10**
Total Debt $1015.2 mill. Due in 5 Yrs $18.9 mill.
LT Debt $996.3 mill. Interest $35 mill.
(12% of Capital)
Leases, Uncapitalized Annual rentals $49.0 mill.

Pension Assets-12/09 $177.3 mill. Oblig. $262.4 mill.
Pfd Stock None

Common Stock 396,940,168 shares as of 7/31/10

MARKET CAP: $18.5 billion (Large Cap)

| 2000 | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 | 2007 | 2008 | 2009 | 2010 | 2011 | | 13-15 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| 2289.4 | 2602.3 | 3011.6 | 3625.3 | 4262.3 | 4871.5 | 5405.6 | 6000.5 | 6718.2 | 6723.1 | **7250** | **7800** | Sales ($mill) | **10150** |
| 23.7% | 24.7% | 24.9% | 24.9% | 25.6% | 26.8% | 27.0% | 28.2% | 28.9% | 31.0% | **30.5%** | **31.5%** | Operating Margin | **33.5%** |
| 109.4 | 172.0 | 186.1 | 229.7 | 250.9 | 289.9 | 331.8 | 366.6 | 387.6 | 385.3 | **397** | **405** | Depreciation ($mill) | **425** |
| 221.0 | 271.8 | 357.1 | 453.5 | 586.5 | 719.1 | 830.4 | 1000.7 | 1147.8 | 1107.4 | **1290** | **1440** | Net Profit ($mill) | **2110** |
| 34.0% | 33.0% | 31.8% | 30.5% | 30.0% | 29.4% | 28.2% | 28.0% | 27.4% | 31.8% | **28.0%** | **28.0%** | Income Tax Rate | **28.0%** |
| 9.7% | 10.4% | 11.9% | 12.5% | 13.8% | 14.8% | 15.4% | 16.7% | 17.1% | 16.5% | **17.8%** | **18.5%** | Net Profit Margin | **20.8%** |
| 379.6 | 459.7 | 443.8 | 547.1 | 1029.1 | 1621.3 | 2182.8 | 3571.9 | 3517.2 | 4410.2 | **6455** | **7650** | Working Cap'l ($mill) | **12915** |
| 876.5 | 720.9 | 491.0 | 18.8 | .7 | 184.2 | - - | - - | - - | - - | **995** | **995** | Long-Term Debt ($mill) | **995** |
| 854.9 | 1056.2 | 1498.2 | 2154.8 | 2752.0 | 3251.8 | 4191.0 | 5378.5 | 5406.7 | 6595.1 | **7400** | **8340** | Shr. Equity ($mill) | **12795** |
| 15.2% | 17.0% | 19.0% | 21.4% | 21.4% | 20.9% | 19.8% | 18.6% | 21.2% | 16.8% | **15.5%** | **15.5%** | Return on Total Cap'l | **15.5%** |
| 25.9% | 25.7% | 23.8% | 21.0% | 21.3% | 22.1% | 19.8% | 18.6% | 21.2% | 16.8% | **17.5%** | **17.5%** | Return on Shr. Equity | **16.5%** |
| 24.4% | 24.2% | 22.5% | 19.9% | 20.3% | 21.0% | 18.7% | 16.9% | 18.7% | 13.8% | **14.0%** | **14.5%** | Retained to Com Eq | **14.0%** |
| 6% | 6% | 6% | 5% | 5% | 5% | 5% | 9% | 12% | 18% | **18%** | **17%** | All Div'ds to Net Prof | **16%** |

**CURRENT POSITION ($MILL.)**

| | 2008 | 2009 | 6/30/10 |
|---|---|---|---|
| Cash Assets | 2195.6 | 2954.8 | 4028.5 |
| Receivables | 1129.5 | 1147.1 | 1108.2 |
| Inventory (LIFO) | 952.7 | 943.0 | 968.2 |
| Other | 701.5 | 806.3 | 794.9 |
| Current Assets | 4979.3 | 5851.2 | 6899.8 |
| Accts Payable | 274.3 | 200.2 | 212.8 |
| Debt Due | 20.5 | 18.0 | 18.9 |
| Other | 1167.3 | 1222.8 | 1063.4 |
| Current Liab. | 1462.1 | 1441.0 | 1295.1 |

**ANNUAL RATES**

| of change (per sh) | Past 10 Yrs. | Past 5 Yrs. | Est'd '07-'09 to '13-'15 |
|---|---|---|---|
| Sales | 16.0% | 12.0% | 8.0% |
| "Cash Flow" | 21.5% | 16.0% | 10.0% |
| Earnings | 22.0% | 18.5% | 12.5% |
| Dividends | 27.0% | 37.5% | 17.0% |
| Book Value | 24.0% | 22.0% | 14.5% |

| Cal-endar | QUARTERLY SALES ($ mill.) Mar.31 | Jun.30 | Sep.30 | Dec.31 | Full Year |
|---|---|---|---|---|---|
| 2007 | 1426 | 1464 | 1453 | 1658 | 6001 |
| 2008 | 1634 | 1713 | 1653 | 1718 | 6718 |
| 2009 | 1602 | 1634 | 1653 | 1834 | 6723 |
| 2010 | 1799 | 1758 | **1833** | **1860** | **7250** |
| 2011 | **1895** | **1935** | **1970** | **2000** | **7800** |

| Cal-endar | EARNINGS PER SHARE A Mar.31 | Jun.30 | Sep.30 | Dec.31 | Full Year |
|---|---|---|---|---|---|
| 2007 | .58 | .61 | .55 | .66 | 2.40 |
| 2008 | .70 | .73 | .66 | .69 | 2.78 |
| 2009 | .71 | .73 | .57 | .76 | 2.77 |
| 2010 | .80 | .80 | **.82** | **.83** | **3.25** |
| 2011 | **.87** | **.90** | **.92** | **.96** | **3.65** |

| Cal-endar | QUARTERLY DIVIDENDS PAID B■ Mar.31 | Jun.30 | Sep.30 | Dec.31 | Full Year |
|---|---|---|---|---|---|
| 2006 | .11 | - - | - - | - - | .11 |
| 2007 | .22 | - - | - - | - - | .22 |
| 2008 | .33 | - - | - - | - - | .33 |
| 2009 | .40 | - - | - - | .10 | .50 |
| 2010 | .15 | .15 | .15 | | |

**BUSINESS:** Stryker Corp. develops, manufactures, and markets Orthopaedic Implants (61% of '09 sales), and MedSurg Equipment (39%). Orthopaedic products include hip, knee, trauma, spinal, and craniomaxillofacial implants. MedSurg includes powered instruments, endoscopic systems, other operating room devices, specialty stretchers, and maternity beds. Physical Therapy Services business sold '07. About 36% of '09 sales were foreign. R&D: 5.0% of '09 sales. '09 depr. rate: 19.6%. Has 18,582 employees. Off. and dir. (incl. Stryker family trust) own 30.7% of stock (3/10 proxy), 3 others aggregate 15.7%. Chairman, President. & CEO: Stephen MacMillan. Inc.: MI. Addr.: 2825 Airview Blvd, Kalamazoo, MI 49002. Telephone: 269-385-2600. Internet: www.stryker.com.

**The top line is on track to post a healthy advance in 2010 at Stryker Corp.** This medical device manufacturer's capital equipment group, MedSurg, has improved considerably in the June quarter, after experiencing a significant cutback in sales activity during the recession. Constrained hospital spending likely froze budgets, but not all purchases can be delayed indefinitely, as demonstrated by buyers entering the market once again. Similarly, shipments in the Orthopaedic Implants division also improved, likely thanks to the resurgence of previously postponed elective procedures .

**Earnings should record a handsome advance, too.** Pricing has held relatively steady despite economic turmoil and competitive pressures, and because of a favorable product mix, margins will likely expand this year. In addition, Stryker has kept a lid on expenses while undertaking a necessary $200 million compliance initiative, offsetting a potential drag on profits. Furthermore, a $750 million share-repurchase program should help support share net over the next several years.

**Stryker's diversified product line is a solid growth platform.** The company has turned a spotlight on device introductions to fill out gaps and broaden the existing portfolio. One bright prospect, a customizable knee offering from business unit OtisMed, is poised for a rollout later this year, contingent on FDA clearance. Also, two new hip offerings are in the works, as are collaborations with newly acquired medical device reprocessor Ascent Healthcare. Moreover, a hearty cash balance should easily fund reseacrch and development initiatives (expected to climb 15% in 2010), or be utilized for outside growth ventures.

**These timely shares are appealing to investors of many stripes.** SYK stock has dropped more than 15% in price since our May review and thus offers an enticing entry point. Substantial capital appreciation potential over the haul to 2013-2015 ought to appeal to the patient set, while short-term accounts will likely enjoy above-average market returns in the coming year. And, with Stryker's solid cash flow generation, investors are likely to enjoy boosts to the dividend as well.

*Mary Beth Wiedenkeller* *August 27, 2010*

(A) Based on average shares through '96; diluted thereafter. Excludes extraordinary gains of $0.03 in 1996. Excludes nonrecurring losses (gains): '98, $0.57; '99, $0.71; '01, $0.01; '02, $0.03; '04, $0.29; '05, $0.11; '06, 13¢; 07, 4¢; '08, 5¢. Next earnings rpt. due mid-October. (B) Dividends paid quarterly beginning with December 2009 payment. (C) Includes intangibles. At 6/30/10: $1586.9 million, $4.00/share. (D) In millions, adjusted for stock splits.

| | |
|---|---|
| Company's Financial Strength | A++ |
| Stock's Price Stability | 90 |
| Price Growth Persistence | 75 |
| Earnings Predictability | 100 |

© 2010, Value Line Publishing, Inc. All rights reserved. Factual material is obtained from sources believed to be reliable and is provided without warranties of any kind. THE PUBLISHER IS NOT RESPONSIBLE FOR ANY ERRORS OR OMISSIONS HEREIN. This publication is strictly for subscriber's own, non-commercial, internal use. No part of it may be reproduced, resold, stored or transmitted in any printed, electronic or other form, or used for generating or marketing any printed or electronic publication, service or product.

To subscribe call 1-800-833-0046.

Snapshot
Quote
**Analyst Research**
Morningstar Rating
Options
Data Interpreter
Valuation Ratios
Financial Statements
Key Ratios
Charts
Dividends & Returns
Company Filings new
Insider Trading
Formatted Report
Print

## Stryker Corporation SYK

**Analyst Report** | Analyst Report Archive | Top Rated Stocks in Sector

by Julie Stralow, CFA

**Analyst Note** 08-18-2010 | by Debbie S. Wang

While Boston Scientific BSX management has indicated the firm is looking into a range of strategic options, including the sale of some of its product lines, it has remained mum about the specifics. Now rumors have surfaced that Boston is in serious negotiations with Stryker SYK to sells its neuromodulation business for $1.4 billion-$1.5 billion. We've pegged the value of Boston's neuromodulation unit at about $1 billion in current indications, so if the rumors wind up being true, Stryker would be paying a substantial premium to what we think the segment is actually worth. In this case, we would consider trimming our fair value estimate for Stryker. Financially, though, Stryker would remain in fine shape, given its current $3.0 billion net cash position. Strategically, we think Boston's neuromodulation unit could provide an interesting hedge for Stryker's exposure to spinal implants. With about 9% of its sales coming from its spine unit in 2009, Stryker has a big exposure to this controversial market, which is coming under pressure from third-party payers outside of stenosis and instability indications. If Stryker can capitalize on the chronic pain indications of neuromodulation, we think it could give practitioners another option for patients with severe lower back pain.

Currently, the neuromodulation market is heavily dominated by Medtronic MDT, followed by St. Jude Medical STJ as the distant second, and Boston has trailed along in third place. Unlike its rivals, Boston has not consistently seen double-digit growth in its neuromodulation business. Even more alarming, the firm has not been investing in the development of this emerging technology, from our perspective. We are only starting to scratch the surface of how this technology can be used to address various health conditions. The neuromodulation market is currently most developed for chronic pain, a condition that crosses neurology, anesthesiology, and spinal surgery. But, there is potential to apply this technology to treatment-resistant depression, Parkinson's disease, obesity, fecal and urinary incontinence, and stroke. These additional applications of neuromodulation would push further into neurology, urology, and gastroenterology. Boston already has established relationships with practitioners of those specialties through its peripheral vascular and endosurgery product lines, but

**Morningstar Rating**
★★★★★

**Stock Price**
As of 08-18-2010
$46.86

**Fair Value Estimate**
$72.00

**Consider Buying**
$50.40

**Consider Selling**
$100.80

**Fair Value Uncertainty**
Medium

**Economic Moat**
Wide

**Stewardship Grade**
**C**

**Bulls Say**

- Stryker's balance sheet is filled with cash. Acquisitions to accelerate growth remain a key priority, but the firm could return value to shareholders by other means, as well.
- International operations in Stryker's MedSurg segment--operating room and other medical equipment--remain relatively small and provide a key growth opportunity.
- New products could boost growth in hips (ADM-X3 and Rejuvenate) and keep growth strong in knees (OtisMed's customization system).
- By acquiring Ascent, a leading reprocessor of single-use medical instruments, Stryker aims to provide a way for hospital administrators to lower

the firm has not done a good job of leveraging those ties to include its neuromodulation business. While Stryker probably wouldn't have any special edge for treating these emerging indications, its strong relationships with spinal surgeons could help it expand substantially in the markets Boston already serves. In the hands of an acquirer willing to push neuromodulation into all potential indications, we estimate Boston's neuromodulation business could be worth at least $1.5 billion, depending on which additional indications are eventually approved.

In the end, though, if Boston does sell this unit, we would probably downgrade its economic moat. We expect neuromodulation technology to be a key growth driver for the next decade as it is applied to treat more chronic conditions. If Boston lacks the technology, it will be left at a substantial competitive disadvantage. There are also rumors that Boston may sell its neurovascular unit. Based on the $2.6 billion Covidien COV recently paid for ev3's roughly $500 million in annual sales, we put Boston's neurovascular business in the ballpark of $1.5 billion. We think either Johnson & Johnson JNJ or C.R. Bard BCR could find that business unit attractive. Finally, from a credit standpoint, the addition of cash from this potential sale would alleviate Boston's refinancing risk over the next several years. As a result, we would consider bumping up Boston's credit rating.

*Julie Stralow, CFA, contributed to this note.*

**Thesis** 05-21-2010 | by Julie Stralow, CFA

Stryker excels in several orthopedic and medical equipment niches. We expect the firm to continue launching innovative new products to help expand these niches and its own profitability even further in the long run.

Around 60% of Stryker's revenue comes from orthopedic implants, where the firm is a top-tier provider of knees and hips and a growing provider of spinal implants. We think the orthopedic industry is very attractive because of its high barriers to success, and Stryker should be a key beneficiary of growth in surgical procedures to repair joints. Demographic trends in developed countries should drive solid volume growth for the industry, as their populations age and suffer from the consequences of obesity trends. Although we are enthusiastic about orthopedic volume growth prospects, some uncertainty exists regarding ongoing pricing levels because of U.S. reform initiatives and growing national budget deficits worldwide, which could cause some key payers to scrutinize medical costs more intensely. However, even in our most dire scenarios, we think Stryker's returns on invested capital should remain higher than capital costs, primarily because of the positive characteristics of the orthopedic implant market.

The balance of Stryker's sales comes from tools and equipment to outfit surgical suites and regular hospital rooms. Stryker is particularly prolific in operating room products, including cutting tools, medical video equipment, and irrigation devices. These tools often complement its orthopedic devices and greatly improve the efficiency of surgical procedures. Stryker is even a top provider of

costs--an important consideration especially in an increasingly cost-conscious health-care environment.

**Bears Say**

- Health-care reform efforts could reduce long-term returns in Stryker's U.S. operations, which accounted for 64% of the firm's business in 2009.
- Although Stryker escaped most of the punishment when the Department of Justice targeted knee and hip providers, it might not be so lucky in future dealings with the DOJ, which has turned its attention to a key growth area for Stryker--the spine market.
- Although all outstanding Food and Drug Administration warning letters recently were lifted, Stryker is still working on improving the quality of its manufacturing operations, and there may be more bumps along the way.

medical beds and emergency equipment, such as stretchers. Although not as fundamentally attractive as implants and somewhat susceptible to economic cycles, these offerings often expand at faster rates than Stryker's orthopedic implant products. In the long run, we think that trend could continue, assuming the company expands as expected in international markets.

With its cash-rich balance sheet and admirable free cash-flow generation, Stryker remains in the enviable position of having many avenues to return value to shareholders. Stryker could significantly boost its dividend or repurchase shares at attractive prices to bolster investor returns with its substantial cash resources. Also, depending on the acquisition target, Stryker could use its big cash position to invest in new technology in fast-growing niches, boosting its growth potential.

**Valuation**

We're keeping our fair value estimate at $72 per share. We assume sales growth rebounds to about 11% compounded annually through 2014. Specifically, we assume the orthopedic business grows 9% compounded annually during those years, which reflects solid growth from knees and hips and acceleration in the spine business as new product candidates are launched successfully. From a low base in 2009, we assume the MedSurg business follows the growth trends of the orthopedic business with a little boost from international expansion, causing 14% compound annual growth in that segment from 2009 to 2014. Our fair value estimate also depends on operating margins staying around 23% through 2012 and then dropping to about 22% after the U.S. device tax is implemented in 2014. These factors should lead to earnings per share increasing about 11% during that period. We discount our assumptions at 9.5%.

**Risk**

Economic concerns have disrupted Stryker's medical equipment segment recently, and caregivers may delay purchases in this segment--especially of big ticket items--in economic downturns. Also, many highly motivated and resource-rich firms compete with Stryker. If the company does not stay near the top of the innovation curve, it risks losing customers to those rivals. In the longer term, third-party payers may need to reduce payments for procedures in order to afford the expected uptick in procedure volume. If payment cuts trickle down to Stryker and it can't make comparable cost reductions, those cuts could damage returns on invested capital.

| **Close Competitors** | TTM Sales $Mil | Market Cap $Mil |
|---|---|---|
| **Stryker Corporation** | **7,045** | **18,525** |
| * Johnson & Johnson | 62,593 | 165,212 |
| * Smith & Nephew PLC | 3,935 | 8,084 |
| * Zimmer Holdings, Inc. | 4,203 | 9,845 |

* Morningstar Analyst Report Available

Data as of 06-30-10

**Strategy**

Stryker hopes to arm hospitals and surgeons with the tools needed to successfully treat patients. Its broad product set includes orthopedic implants, operating room equipment, and medical furniture. By interacting with many departments in the hospital, Stryker aims to become a top supplier to medical caregivers. It also aims to acquire new businesses to ramp up growth and diversify sales.

**Management & Stewardship**

Although we think Stryker's stewards employ fair practices, outside shareholders should be aware of how little control they may have on Stryker's strategic direction. Stephen MacMillan heads the firm's executive team and board, which we think remains insulated. Even though the majority of the board pass U.S. independence standards; we think the average tenure on the board, a director's consulting relationship with Stryker, and the founding family's board seat and voting power override that litmus test. Because of those factors, the board's interests may not necessarily be naturally aligned with most shareholders' interests. Also, though we're glad variable compensation, such as bonuses and stock-related rewards, make up the vast majority of executive compensation, we'd prefer to see those rewards based on returns on invested capital or free cash flow rather than earnings per share, which can be easily manipulated and may not be a true measure of value creation. We do applaud Stryker's disclosure surrounding compensation and financial performance, however, and we find Stryker's annual orthopedic market report especially valuable.

**Profile**

Stryker develops, manufactures, and markets medical devices and equipment for use primarily in orthopedic procedures. The firm generates most of its revenue from reconstructive implants, such as knees and hips, but serves a variety of other orthopedic niches, including spine. Stryker also offers a wide range of operating room equipment and tools used for orthopedic and other procedures. Hospital beds and stretchers account for a portion of Stryker's sales, too.

**Growth**

We think new product launches and procedure growth should help Stryker grow 11% compounded annually through 2014. Acquisitions could add to that rate.

**Profitability**

Through major cost-control efforts, operating margins in recent quarters have risen past our long-term assumption of 22%. We think reform initiatives and increasing regulatory requirements could constrain Stryker's margins in the long run.

**Financial Health**

Stryker ended March with $2.9 billion in net cash. With those substantial resources and ongoing cash flow, we expect it to return more value to shareholders or make acquisitions in fast-growing niches.

Authors can be reached at analyst feedback.

Morningstar's editorial policies prohibit analysts from owning stocks they cover. Find out more about Morningstar's editorial policies here.

Morningstar Ratings and Morningstar Risk are updated daily.

Show Data Definitions | Ticker Lookup

**Contact us**. Please read our User's Agreement and Troubleshooting documents.
© 2010 Morningstar, Inc. All rights reserved.