

STRYKER CORP  
Form 10-Q  
April 24, 2019

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT  
OF 1934

For the quarterly period ended March 31, 2019

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF  
1934

Commission file number: 000-09165

STRYKER CORPORATION

(Exact name of registrant as specified in its charter)

Michigan

38-1239739

(State of incorporation)

(I.R.S. Employer Identification No.)

2825 Airview Boulevard Kalamazoo,

49002

Michigan

(Address of principal executive offices) (Zip Code)

(269) 385-2600

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. YES

NO

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). YES  NO

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer  Accelerated filer

Non-accelerated filer  Small reporting company

Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). YES  NO

There were 373,810,085 shares of Common Stock, \$0.10 par value, on March 31, 2019.

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## STRYKER CORPORATION 2019 First Quarter Form 10-Q

## PART I – FINANCIAL INFORMATION

## ITEM 1. FINANCIAL STATEMENTS

Stryker Corporation and Subsidiaries

## CONSOLIDATED STATEMENTS OF EARNINGS (Unaudited)

|  | Three Months |         |
|--|--------------|---------|
|  | 2019         | 2018    |
| Net sales                                      | \$3,516      | \$3,241 |
| Cost of sales                                  | 1,233        | 1,104   |
| Gross profit                                   | \$2,283      | \$2,137 |
| Research, development and engineering expenses | 225          | 204     |
| Selling, general and administrative expenses   | 1,403        | 1,236   |
| Recall charges                                 | 13           | 4       |
| Amortization of intangible assets              | 114          | 102     |
| Total operating expenses                       | \$1,755      | \$1,546 |
| Operating income                               | \$528        | \$591   |
| Other income (expense), net                    | (48 )        | (49 )   |
| Earnings before income taxes                   | \$480        | \$542   |
| Income taxes                                   | 68           | 99      |
| Net earnings                                   | \$412        | \$443   |

## Net earnings per share of common stock:

|         |        |        |
|---------|--------|--------|
| Basic   | \$1.10 | \$1.18 |
| Diluted | \$1.09 | \$1.16 |

## Weighted-average shares outstanding (in millions):

|   |       |       |
|---|-------|-------|
| Basic                                     | 373.3 | 374.0 |
| Effect of dilutive employee stock options | 6.0   | 6.7   |
| Diluted                                   | 379.3 | 380.7 |

Cash dividends declared per share of common stock \$0.52 \$0.47

Anti-dilutive shares excluded from the calculation of dilutive employee stock options were de minimis in all periods.

## CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (Unaudited)

|   | Three Months |       |
|---|--------------|-------|
|   | 2019         | 2018  |
| Net earnings  | \$412        | \$443 |
| Other comprehensive income (loss), net of tax:      |              |       |
| Marketable securities                               | 1            | (1 )  |
| Pension plans                                       | (4 )         | (6 )  |
| Unrealized gains (losses) on designated hedges      | (16 )        | 15    |
| Financial statement translation                     | 85           | 35    |
| Total other comprehensive income (loss), net of tax | \$66         | \$43  |
| Comprehensive income                                | \$478        | \$486 |

See accompanying notes to Consolidated Financial Statements.

Dollar amounts are in millions except per share amounts or as otherwise specified. 1



## STRYKER CORPORATION 2019 First Quarter Form 10-Q

## CONSOLIDATED BALANCE SHEETS

|  | March 31    | December  |
|--|-------------|-----------|
|  | 2019        | 31        |
|  | (Unaudited) | 2018      |
| Assets   |             |           |
| Current assets   |             |           |
| Cash and cash equivalents                                  | \$ 1,674    | \$ 3,616  |
| Marketable securities                                      | 84          | 83        |
| Accounts receivable, less allowance of \$67 (\$64 in 2018) | 2,284       | 2,332     |
| Inventories:   |             |           |
| Materials and supplies                                     | 608         | 606       |
| Work in process  | 178         | 149       |
| Finished goods   | 2,278       | 2,200     |
| Total inventories  | \$ 3,064    | \$ 2,955  |
| Prepaid expenses and other current assets                  | 782         | 747       |
| Total current assets                                       | \$ 7,888    | \$ 9,733  |
| Property, plant and equipment:                             |             |           |
| Land, buildings and improvements                           | 1,021       | 1,041     |
| Machinery and equipment                                    | 3,321       | 3,236     |
| Total property, plant and equipment                        | \$ 4,342    | \$ 4,277  |
| Less accumulated depreciation                              | 2,045       | 1,986     |
| Property, plant and equipment, net                         | \$ 2,297    | \$ 2,291  |
| Goodwill   | 8,710       | 8,563     |
| Other intangibles, net                                     | 4,240       | 4,163     |
| Noncurrent deferred income tax assets                      | 1,631       | 1,678     |
| Other noncurrent assets                                    | 1,171       | 801       |
| Total assets   | \$ 25,937   | \$ 27,229 |
| Liabilities and shareholders' equity                       |             |           |
| Current liabilities  |             |           |
| Accounts payable   | \$ 619      | \$ 646    |
| Accrued compensation                                       | 531         | 917       |
| Income taxes payable                                       | 154         | 158       |
| Dividend payable   | 192         | 192       |
| Accrued expenses and other liabilities                     | 1,696       | 1,521     |
| Current maturities of debt                                 | 521         | 1,373     |
| Total current liabilities                                  | \$ 3,713    | \$ 4,807  |
| Long-term debt, excluding current maturities               | 7,950       | 8,486     |
| Income taxes   | 1,218       | 1,228     |
| Other noncurrent liabilities                               | 1,363       | 978       |
| Total liabilities  | \$ 14,244   | \$ 15,499 |
| Shareholders' equity                                       |             |           |
| Common stock, \$0.10 par value                             | 37          | 37        |
| Additional paid-in capital                                 | 1,538       | 1,559     |
| Retained earnings  | 10,683      | 10,765    |
| Accumulated other comprehensive loss                       | (565)       | (631)     |
| Total shareholders' equity                                 | \$ 11,693   | \$ 11,730 |
| Total liabilities and shareholders' equity                 | \$ 25,937   | \$ 27,229 |

See accompanying notes to Consolidated Financial Statements.

Dollar amounts are in millions except per share amounts or as otherwise specified. 2

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## STRYKER CORPORATION 2019 First Quarter Form 10-Q

## CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY (Unaudited)

|   | Three Months<br>2019 |          | Three Months<br>2018 |         |
|---|----------------------|----------|----------------------|---------|
|   | Shares               | Amount   | Shares               | Amount  |
| Common stock  |                      |          |                      |         |
| Beginning   | 374.4                | \$37     | 374.4                | \$37    |
| Issuance of common stock under stock option and benefit plans | 1.3                  | —        | 1.2                  | —       |
| Repurchase of common stock                                    | (1.9)                | —        | (1.9)                | —       |
| Ending  | 373.8                | \$37     | 373.7                | \$37    |
| Additional paid-in capital                                    |                      |          |                      |         |
| Beginning   |                      | \$1,559  |                      | \$1,496 |
| Issuance of common stock under stock option and benefit plans | (48)                 | )        | (32)                 | )       |
| Repurchase of common stock                                    | (8)                  | )        | (7)                  | )       |
| Share-based compensation                                      | 35                   |          | 29                   |         |
| Ending  |                      | \$1,538  |                      | \$1,486 |
| Retained earnings   |                      |          |                      |         |
| Beginning   |                      | \$10,765 |                      | \$8,986 |
| Cumulative effect of accounting changes                       |                      | —        |                      | (759)   |
| Net earnings  |                      | 412      |                      | 443     |
| Repurchase of common stock                                    | (299)                | )        | (293)                | )       |
| Cash dividends declared                                       | (195)                | )        | (176)                | )       |
| Ending  |                      | \$10,683 |                      | \$8,201 |
| Accumulated other comprehensive (loss) income                 |                      |          |                      |         |
| Beginning   |                      | \$(631)  |                      | \$(553) |
| Other comprehensive income (loss)                             |                      | 66       |                      | 43      |
| Ending  |                      | \$(565)  |                      | \$(510) |
| Total Stryker shareholders' equity                            |                      | \$11,693 |                      | \$9,214 |
| Non-controlling interest                                      |                      |          |                      |         |
| Beginning   |                      | \$—      |                      | \$14    |
| Interest purchased  |                      | —        |                      | (6)     |
| Net earnings attributable to noncontrolling interest          |                      | —        |                      | —       |
| Foreign currency exchange translation adjustment              |                      | —        |                      | 1       |
| Ending  |                      | \$—      |                      | \$9     |
| Total shareholders' equity                                    |                      | \$11,693 |                      | \$9,223 |

See accompanying notes to Consolidated Financial Statements.

Dollar amounts are in millions except per share amounts or as otherwise specified. 3

## STRYKER CORPORATION 2019 First Quarter Form 10-Q

## CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)

|   | Three Months |          |
|---|--------------|----------|
|   | 2019         | 2018     |
| Operating activities  |              |          |
| Net earnings  | \$412        | \$443    |
| Adjustments to reconcile net earnings to net cash provided by operating activities: |              |          |
| Depreciation  | 76           | 74       |
| Amortization of intangible assets   | 114          | 102      |
| Share-based compensation  | 35           | 29       |
| Recall charges  | 13           | 4        |
| Sale of inventory stepped-up to fair value at acquisition                           | 24           | 3        |
| Changes in operating assets and liabilities:  |              |          |
| Accounts receivable   | 50           | 139      |
| Inventories   | (139 )       | (144 )   |
| Accounts payable  | (12 )        | 33       |
| Accrued expenses and other liabilities  | (166 )       | (306 )   |
| Recall-related payments   | (20 )        | (28 )    |
| Income taxes  | 9            | 48       |
| Other, net  | (83 )        | (100 )   |
| Net cash provided by operating activities   | \$313        | \$297    |
| Investing activities  |              |          |
| Acquisitions, net of cash acquired  | (180 )       | (704 )   |
| Purchases of marketable securities  | (20 )        | (77 )    |
| Proceeds from sales of marketable securities  | 19           | 53       |
| Purchases of property, plant and equipment  | (122 )       | (121 )   |
| Net cash used in investing activities   | \$(303 )     | \$(849 ) |
| Financing activities  |              |          |
| Proceeds and payments on short-term borrowings, net                                 | (12 )        | 99       |
| Proceeds from issuance of long-term debt  | —            | 595      |
| Payments on long-term debt  | (1,341 )     | —        |
| Dividends paid  | (195 )       | (176 )   |
| Repurchases of common stock   | (307 )       | (300 )   |
| Cash paid for taxes from withheld shares  | (97 )        | (75 )    |
| Payments to purchase noncontrolling interest  | —            | (5 )     |
| Other financing, net  | 5            | 7        |
| Net cash (used in) provided by financing activities                                 | \$(1,947)    | \$145    |
| Effect of exchange rate changes on cash and cash equivalents                        | (5 )         | 44       |
| Change in cash and cash equivalents   | \$(1,942)    | \$(363 ) |
| Cash and cash equivalents at beginning of period                                    | 3,616        | 2,542    |
| Cash and cash equivalents at end of period  | \$1,674      | \$2,179  |

See accompanying notes to Consolidated Financial Statements.

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## STRYKER CORPORATION 2019 First Quarter Form 10-Q

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

## NOTE 1 - BASIS OF PRESENTATION

## General Information

Management believes the accompanying unaudited Consolidated Financial Statements contain all adjustments, including normal recurring items, considered necessary to fairly present the financial position of Stryker Corporation and its consolidated subsidiaries (the "Company," "we," "us" or "our") on March 31, 2019 and the results of operations for the three months 2019. The results of operations included in these Consolidated Financial Statements may not necessarily be indicative of our annual results. These statements should be read in conjunction with our Annual Report on Form 10-K for 2018.

Certain prior year amounts have been reclassified to conform with current year presentation in our Consolidated Statements of Cash Flows.

## New Accounting Pronouncements Not Yet Adopted

We evaluate all Accounting Standards Updates (ASUs) issued by the Financial Accounting Standards Board (FASB) for consideration of their applicability. ASUs not included in our disclosures were assessed and determined to be either not applicable or are not expected to have a material impact on our Consolidated Financial Statements.

In August 2018 the FASB issued ASU 2018-15, Intangibles - Goodwill and Other - Internal Use Software - Customer's Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a Service Contract, which amends the requirements for capitalizing implementation costs incurred in a hosting arrangement that is a service contract to align with the requirements for capitalizing implementation costs incurred to develop or obtain internal-use software. The update is effective for fiscal years beginning after December 15, 2020, including interim periods within those fiscal years. Early adoption is permitted. We are in the process of evaluating the impact on our Consolidated Financial Statements and the timing of adoption of this update.

## Accounting Pronouncements Recently Adopted

On January 1, 2019 we adopted ASU 2016-02, Leases, and related amendments (ASC 842), which require lease assets and liabilities to be recorded on the balance sheet for leases with terms greater than twelve months. Refer to Note 6 for further information.

On January 1, 2019 we adopted ASU 2017-12, Derivatives and Hedging - Targeted Improvements to Accounting for Hedging Activities, which amends and simplifies hedge accounting guidance, as well as improves presentation and disclosure to align the economic effects of risk management strategies in the financial statements. The adoption of this update did not have a material impact on our Consolidated Financial Statements.

## NOTE 2 - REVENUE RECOGNITION

Our policies for recognizing sales have not changed from those described in our Annual Report on Form 10-K for 2018.

We disaggregate our net sales by product line and geography for each of our segments as we believe it best depicts how the nature, amount, timing and certainty of our net sales and cash flows are affected by economic factors.

## Net Sales by Product Line

|                        | Three Months |         |
|------------------------|--------------|---------|
|                        | 2019         | 2018    |
| Orthopaedics:          |              |         |
| Knees                  | \$439        | \$419   |
| Hips                   | 336          | 331     |
| Trauma and Extremities | 396          | 389     |
| Other                  | 79           | 77      |
|                        | \$1,250      | \$1,216 |
| MedSurg:               |              |         |
| Instruments            | \$478        | \$412   |
| Endoscopy              | 470          | 444     |
| Medical                | 531          | 511     |

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|                |         |         |
|----------------|---------|---------|
| Sustainability | 65      | 60      |
|                | \$1,544 | \$1,427 |

Neurotechnology and Spine:

|                 |       |       |
|-----------------|-------|-------|
| Neurotechnology | \$465 | \$410 |
| Spine           | 257   | 188   |
|                 | \$722 | \$598 |

|       |         |         |
|-------|---------|---------|
| Total | \$3,516 | \$3,241 |
|-------|---------|---------|

Net Sales by Geography

|                            | Three Months 2019 |               | Three Months 2018 |               |
|----------------------------|-------------------|---------------|-------------------|---------------|
|                            | United States     | International | United States     | International |
| Orthopaedics:              |                   |               |                   |               |
| Knees                      | \$320             | \$ 119        | \$301             | \$ 118        |
| Hips                       | 213               | 123           | 205               | 126           |
| Trauma and Extremities     | 254               | 142           | 245               | 144           |
| Other                      | 63                | 16            | 63                | 14            |
|                            | \$850             | \$ 400        | \$814             | \$ 402        |
| MedSurg:                   |                   |               |                   |               |
| Instruments                | \$381             | \$ 97         | \$316             | \$ 96         |
| Endoscopy                  | 376               | 94            | 349               | 95            |
| Medical                    | 416               | 115           | 381               | 130           |
| Sustainability             | 64                | 1             | 60                | —             |
|                            | \$1,237           | \$ 307        | \$1,106           | \$ 321        |
| Neurotechnology and Spine: |                   |               |                   |               |
| Neurotechnology            | \$297             | \$ 168        | \$256             | \$ 154        |
| Spine                      | 195               | 62            | 138               | 50            |
|                            | \$492             | \$ 230        | \$394             | \$ 204        |
| Total                      | \$2,579           | \$ 937        | \$2,314           | \$ 927        |

Contract Assets and Liabilities

On March 31, 2019 there were no contract assets recorded on our Consolidated Balance Sheets.

Our contract liabilities arise as a result of consideration received from customers at inception of contracts for certain businesses or where the timing of billing for services precedes satisfaction of our performance obligations. We generally satisfy performance obligations within one year from the contract inception date. Our contract liabilities were \$331 and \$327 on March 31, 2019 and December 31, 2018.

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## STRYKER CORPORATION 2019 First Quarter Form 10-Q

## NOTE 3 - ACCUMULATED OTHER COMPREHENSIVE (LOSS) INCOME (AOCI)

| Three Months 2019     | Marketable<br>Securities | Pension<br>Plans | Hedges  | Financial<br>Statement<br>Translation | Total   |
|-----------------------|--------------------------|------------------|---------|---------------------------------------|---------|
| Beginning             | \$ (4 )                  | \$(137 )         | \$ 50   | \$ (540 )                             | \$(631) |
| OCI                   | 1                        | (6 )             | (19 )   | 94                                    | 70      |
| Income taxes          | —                        | 1                | 6       | (9 )                                  | (2 )    |
| Reclassifications to: |                          |                  |         |                                       |         |
| Cost of sales         | —                        | —                | (2 )    | —                                     | (2 )    |
| Other expense         | —                        | 1                | —       | —                                     | 1       |
| Income taxes          | —                        | —                | (1 )    | —                                     | (1 )    |
| Net OCI               | \$ 1                     | \$(4 )           | \$(16 ) | \$ 85                                 | \$66    |
| Ending                | \$ (3 )                  | \$(141 )         | \$ 34   | \$ (455 )                             | \$(565) |

| Three Months 2018     | Marketable<br>Securities | Pension<br>Plans | Hedges | Financial<br>Statement<br>Translation | Total   |
|-----------------------|--------------------------|------------------|--------|---------------------------------------|---------|
| Beginning             | \$ (4 )                  | \$(134 )         | \$ 28  | \$ (443 )                             | \$(553) |
| OCI                   | (1 )                     | (10 )            | 21     | 23                                    | 33      |
| Income taxes          | —                        | 1                | (5 )   | 12                                    | 8       |
| Reclassifications to: |                          |                  |        |                                       |         |
| Cost of sales         | —                        | —                | (1 )   | —                                     | (1 )    |
| Other expense         | —                        | 2                | —      | —                                     | 2       |
| Income taxes          | —                        | 1                | —      | —                                     | 1       |
| Net OCI               | \$ (1 )                  | \$(6 )           | \$ 15  | \$ 35                                 | \$43    |
| Ending                | \$ (5 )                  | \$(140 )         | \$ 43  | \$ (408 )                             | \$(510) |

## NOTE 4 - DERIVATIVE INSTRUMENTS

## Foreign Currency Hedges

We use operational and economic hedges, foreign currency exchange forward contracts, net investment hedges (both derivative and non-derivative financial instruments) and interest rate derivative instruments to manage the impact of currency exchange and interest rate fluctuations on earnings and cash flow. We do not enter into derivative instruments for speculative purposes. We have not changed our hedging strategies, accounting practices or objectives from those disclosed in our Annual Report on Form 10-K for 2018.

| March 2019                   | Designated | Non-Designated | Total   |
|------------------------------|------------|----------------|---------|
| Gross notional amount        | \$ 844     | \$ 4,529       | \$5,373 |
| Maximum term in days         |            |                | 586     |
| Fair value:                  |            |                |         |
| Other current assets         | \$ 8       | \$ 100         | \$108   |
| Other noncurrent assets      | —          | 16             | 16      |
| Other current liabilities    | (12 )      | (5 )           | (17 )   |
| Other noncurrent liabilities | (1 )       | —              | (1 )    |
| Total fair value             | \$ (5 )    | \$ 111         | \$106   |
| December 2018                | Designated | Non-Designated | Total   |
| Gross notional amount        | \$ 870     | \$ 5,466       | \$6,336 |
| Maximum term in days         |            |                | 586     |
| Fair value:                  |            |                |         |
| Other current assets         | \$ 15      | \$ 28          | \$43    |
| Other noncurrent assets      | 1          | 33             | 34      |
| Other current liabilities    | (5 )       | (15 )          | (20 )   |
| Other noncurrent liabilities | —          | —              | —       |

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Total fair value \$ 11 \$ 46 \$57

On March 31, 2019 the total after tax amount in AOCI related to our designated net investment hedges was \$11. We evaluate the effectiveness of our net investment hedges quarterly. We have not recognized any ineffectiveness in 2019.

We are exposed to credit loss in the event of nonperformance by our counterparties on our outstanding derivative instruments but do not anticipate nonperformance by any of our counterparties. Should

a counterparty default, our maximum loss exposure is the asset balance of the instrument.

Net Currency Exchange Rate Gains (Losses)

|                             |            |
|-----------------------------|------------|
|                             | Three      |
|                             | Months     |
| Recorded in:                | 2019 2018  |
| Cost of sales               | \$2 \$1    |
| Other income (expense), net | (2 ) (2 )  |
| Total                       | \$— \$ (1) |

Pretax gains (losses) on derivatives designated as hedges recorded in AOCI that are expected to be reclassified to earnings within 12 months of the balance sheet date are (\$3) and \$13 on March 31, 2019 and December 31, 2018. This reclassification is primarily due to the sale of inventory that includes previously hedged purchases. There were de minimis ineffective portions of derivatives, which are included in the table above.

Interest Rate Risk

On March 31, 2019 there are no open cash flow or fair value interest rate hedges.

NOTE 5 - FAIR VALUE MEASUREMENTS

Our policies for managing risk related to foreign currency, interest rates, credit and markets and our process for determining fair value have not changed from those described in our Annual Report on Form 10-K for 2018.

There were no significant transfers into or out of any level in 2019.

| Assets Measured at Fair Value                  | March 2019 | December 2018 |
|--|------------|---------------|
| Cash and cash equivalents                      | \$1,674    | \$ 3,616      |
| Trading marketable securities                  | 132        | 118           |
| Level 1 - Assets                               | \$1,806    | \$ 3,734      |
| Available-for-sale marketable securities:      |            |               |
| Corporate and asset-backed debt securities     | \$36       | \$ 38         |
| United States agency debt securities           | 10         | 11            |
| United States Treasury debt securities         | 28         | 23            |
| Certificates of deposit                        | 10         | 11            |
| Total available-for-sale marketable securities | \$84       | \$ 83         |
| Foreign currency exchange forward contracts    | 124        | 77            |
| Level 2 - Assets                               | \$208      | \$ 160        |
| Total assets measured at fair value            | \$2,014    | \$ 3,894      |
| Liabilities Measured at Fair Value             | March 2019 | December 2018 |
| Deferred compensation arrangements             | \$132      | \$ 118        |
| Level 1 - Liabilities                          | \$132      | \$ 118        |
| Foreign currency exchange forward contracts    | \$18       | \$ 20         |
| Level 2 - Liabilities                          | \$18       | \$ 20         |
| Contingent consideration:                      |            |               |
| Beginning                                      | \$117      | \$ 32         |
| Additions                                      | 128        | 77            |
| Change in estimate                             | —          | 15            |
| Settlements                                    | (1 )       | (7 )          |
| Ending   | \$244      | \$ 117        |

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|  |       |        |
|--|-------|--------|
| Level 3 - Liabilities                    | \$244 | \$ 117 |
| Total liabilities measured at fair value | \$394 | \$ 255 |

Fair Value of Available for Sale Securities by Maturity

|  | March | December |
|--|-------|----------|
|  | 2019  | 2018     |

|                         |       |       |
|-------------------------|-------|-------|
| Due in one year or less | \$ 42 | \$ 51 |
|-------------------------|-------|-------|

|  |       |       |
|--|-------|-------|
| Due after one year through three years | \$ 42 | \$ 32 |
|--|-------|-------|

On March 31, 2019 and December 31, 2018 the aggregate difference between the cost and fair value of available-for-sale marketable securities was nominal. Interest and marketable securities income recorded in other income (expense), net, was \$39 and \$23 in the three months 2019 and 2018.

Dollar amounts are in millions except per share amounts or as otherwise specified. 6

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## STRYKER CORPORATION 2019 First Quarter Form 10-Q

Our investments in available-for-sale marketable securities had a minimum credit quality rating of A2 (Moody's), A (Standard & Poor's) and A (Fitch). We do not plan to sell the investments, and it is not more likely than not that we will be required to sell the investments before recovery of their amortized cost basis, which may be maturity. We do not consider these investments to be other-than-temporarily impaired on March 31, 2019. On March 31, 2019 the majority of our investments with unrealized losses that were not deemed to be other-than-temporarily impaired were in a continuous unrealized loss position for less than twelve months, and the losses were not material.

## Securities in a Continuous Unrealized Loss Position

|                            | Number of Investments | Fair Value |
|----------------------------|-----------------------|------------|
| Corporate and asset-backed | 29                    | \$ 13      |
| United States agency       | 6                     | 8          |
| United States Treasury     | 13                    | 12         |
| Certificates of deposit    | 1                     | 1          |
| Total                      | 49                    | \$ 34      |

## NOTE 6 - CONTINGENCIES AND COMMITMENTS

We are involved in various ongoing proceedings, legal actions and claims arising in the normal course of business, including proceedings related to product, labor, intellectual property and other matters that are more fully described below. The outcomes of these matters will generally not be known for prolonged periods of time. In certain of the legal proceedings, the claimants seek damages as well as other compensatory and equitable relief that could result in the payment of significant claims and settlements and/or the imposition of injunctions or other equitable relief. For legal matters for which management had sufficient information to reasonably estimate our future obligations, a liability representing management's best estimate of the probable loss, or the minimum of the range of probable losses when a best estimate within the range is not known, is recorded. The estimates are based on consultation with legal counsel, previous settlement experience and settlement strategies. If actual outcomes are less favorable than those estimated by management, additional expense may be incurred, which could unfavorably affect future operating results. We are self-insured for product liability claims and expenses. The ultimate cost to us with respect to product liability claims could be materially different than the amount of the current estimates and accruals and could have a material adverse effect on our financial position, results of operations and cash flows.

In 2010 we filed a lawsuit in federal court against Zimmer Biomet Holdings, Inc. (Zimmer), alleging that a Zimmer product infringed on three of our patents. In 2013 following a jury trial favorable to us, the trial judge entered a final judgment that, among other things, awarded us damages of \$76 and ordered Zimmer to pay us enhanced damages. Zimmer appealed this ruling. In December 2014 the Federal Circuit affirmed the damages awarded to us, reversed the order for enhanced damages and remanded the issue of attorney fees to the trial court. In May 2015 the trial court entered a stipulated judgment that, among other things, required Zimmer to pay us the base amount of damages and interest, while the issues of enhanced damages and attorney fees continue to be pursued. In June 2015 we recorded a \$54 gain, net of legal costs, which was recorded within selling, general and administrative expenses. On June 13, 2016 the United States Supreme Court vacated the decision of the Federal Circuit that reversed our judgment for enhanced damages and remanded the case to the Federal Circuit to reconsider the issue. On September 12, 2016 the Federal Circuit issued an opinion that, among other things, remanded the issue of enhanced damages to the trial court. On July 12, 2017 the trial court reaffirmed its award of enhanced damages and entered a judgment

of \$164 in our favor. Zimmer appealed, and on December 10, 2018 the Federal Circuit affirmed the decision. Zimmer filed a petition on January 23, 2019 to seek a rehearing of this ruling by the entire Federal Circuit. On March 19, 2019 the Federal Circuit denied Zimmer's petition for a rehearing. Zimmer conditionally paid us \$167 while it considers its options for additional appeals. Zimmer's opportunity for further appeals expires on June 17, 2019.

## Recall Matters

In June 2012 we voluntarily recalled our Rejuvenate and ABG II Modular-Neck hip stems and terminated global distribution of these hip products. Product liability lawsuits relating to this voluntary recall have been filed against us. In November 2014 we entered into a settlement agreement to compensate eligible United States patients who had

revision surgery prior to November 3, 2014 and in December 2016 the settlement program was extended to patients who had revision surgery prior to December 19, 2016. We continue to offer support for recall-related care and reimburse patients who are not eligible to enroll in the settlement program for testing and treatment services, including any necessary revision surgeries. In addition, there are remaining lawsuits that we will continue to defend against. In August 2016 and May 2018 we voluntarily recalled certain lot-specific sizes and offsets of LFIT Anatomic CoCr V40 Femoral Heads. Product liability lawsuits and claims relating to this voluntary recall have been filed against us. In November 2018 we entered into a settlement agreement to resolve a significant number of claims and lawsuits related to the recalls. The specific terms of the settlement agreement, including the financial terms, are confidential. We have incurred, and expect to incur in the future, costs associated with the settlement of these matters. Based on the information that has been received, we have estimated the remaining range of probable loss to resolve these matters globally to be approximately \$250 to \$470. We have recorded charges to earnings representing the minimum of the range of probable loss. The final outcomes of these matters are dependent on many factors that are difficult to predict. Accordingly, the ultimate cost to entirely resolve these matters globally may be materially different than the amount of our current estimate and accruals and could have a material adverse effect on our results of operations and cash flows.

#### Leases

We lease various manufacturing, warehousing and distribution facilities, administrative and sales offices as well as equipment under operating leases. We evaluate our contracts to identify leases, which is generally if there is an identified asset and we have the right to direct the use of and obtain substantially all of the economic benefit from the use of the identified asset. Certain of our lease agreements contain rent escalation clauses (including index-based escalations), rent holidays, capital improvement funding or other lease concessions. We recognize our minimum rental expense on a straight-line basis over the term of the lease beginning with the date of initial control of the asset. With the adoption of ASC 842 we recognized all leases with terms greater than twelve months in duration on our Consolidated Balance Sheets as right-of-use assets and lease liabilities of approximately \$350 as of January 1, 2019. We adopted the standard using the prospective approach and did not retrospectively apply to prior periods. Right-of-use assets are recorded in Other noncurrent assets on our Consolidated Balance Sheets. Current and non-current lease liabilities are recorded in Accrued expenses and other liabilities and Other noncurrent liabilities, respectively, on our Consolidated Balance Sheets.

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## STRYKER CORPORATION 2019 First Quarter Form 10-Q

We have made certain assumptions and judgments when applying ASC 842, the most significant of which are: We elected the package of practical expedients available for transition which allow us to not reassess whether expired or existing contracts contain leases under the new definition of a lease, lease classification for expired or existing leases and whether previously capitalized initial direct costs would qualify for capitalization under ASC 842.

- We did not elect to use hindsight when considering judgments and estimates such as assessments of lessee options to extend or terminate a lease or purchase the underlying asset.

For all asset classes, we elected to not recognize a right-of-use asset and lease liability for short-term leases.

For all asset classes, we elected to not separate non-lease components from lease components to which they relate and have accounted for the combined lease and non-lease components as a single lease component.

The determination of the discount rate used in a lease is our incremental borrowing rate which is based on what we would normally pay to borrow on a collateralized basis over a similar term an amount equal to the lease payments.

|                                |               |
|--------------------------------|---------------|
| Leases                         | March<br>2019 |
| Right-of-use assets            | \$ 355        |
| Lease liabilities, current     | 89            |
| Lease liabilities, non-current | 258           |

## Other information

|                                       |              |
|---------------------------------------|--------------|
| Weighted-average remaining lease term | 5.5<br>years |
| Weighted-average discount rate        | 3.63 %       |

|                      |                                  |
|----------------------|----------------------------------|
| Operating lease cost | Three<br>Months<br>2019<br>\$ 34 |
|----------------------|----------------------------------|

## NOTE 7 - ACQUISITIONS

We acquire stock in companies and various assets that continue to support our capital deployment and product development strategies. Cash paid for acquisitions, net of cash acquired, was \$180 and \$704 in the three months 2019 and 2018. Acquisition and integration related charges, including the amortization of inventory stepped up to fair value, was \$138 and \$17 in the three months 2019 and 2018.

In March 2019 we completed the acquisition of OrthoSpace, Ltd. for total cash consideration of \$110 with future milestone payments of up to an additional \$110. OrthoSpace is a medical device company specializing in orthopaedic biodegradable technology for the treatment of irreparable rotator cuff tears.

In November 2018 we completed the acquisition of K2M Group Holdings, Inc. (K2M) for \$27.50 per share, or an aggregate purchase price of approximately \$1,380. K2M is a global leader of complex spine and minimally invasive solutions focused on achieving three-dimensional Total Body Balance. K2M is part of our Spine business within Neurotechnology and Spine. Goodwill attributable to the acquisition is not deductible for tax purposes.

In February 2018 we completed the acquisition of Entellus Medical, Inc. (Entellus) for \$24.00 per share, or an aggregate purchase price of \$697, net of cash acquired. Entellus is focused on delivering superior patient and physician experiences through products designed for the minimally invasive treatment of various ear, nose and throat (ENT) disease states. Entellus is part of our Neurotechnology business within Neurotechnology and Spine.

Goodwill attributable to the acquisition is not deductible for tax purposes.

The purchase price allocation for K2M is preliminary and is based on estimates and assumptions that are subject to change within the measurement period. The purchase price allocation for the acquisition of Entellus was completed in the three months 2019.

Purchase Price Allocation of Acquired Net Assets



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|  | 2018    |          |
|--|---------|----------|
|  | K2M     | Entellus |
| Tangible assets:                           |         |          |
| Accounts receivable                        | \$67    | \$ 17    |
| Inventory                                  | 136     | 14       |
| Other assets                               | 118     | 62       |
| Contingent consideration                   | —       | (79 )    |
| Other liabilities                          | (247 )  | (76 )    |
| Intangible assets:                         |         |          |
| Customer relationship                      | 34      | 33       |
| Distributor relationship                   | 1       | —        |
| Trade name                                 | 10      | —        |
| Developed technology and patents           | 473     | 261      |
| Internally developed software              | 2       | —        |
| Goodwill                                   | 786     | 465      |
| Purchase price, net of cash acquired       | \$1,380 | \$ 697   |
| Weighted-average life of intangible assets | 14      | 16       |
| Estimated Amortization                     |         |          |
| Expense                                    |         |          |
| Remainder                                  |         |          |
| of   | 2020    | 2021     |
| 2019                                       | 2022    | 2023     |
| \$333                                      | \$422   | \$409    |
| \$401                                      | \$381   |          |

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## STRYKER CORPORATION 2019 First Quarter Form 10-Q

## NOTE 8 - DEBT AND CREDIT FACILITIES

In January 2019 we repaid \$500 of our senior unsecured notes with a coupon of 1.800% that were due on January 15, 2019. In March 2019 we repaid \$750 of our senior unsecured notes with a coupon of 2.000% that were due on March 8, 2019. Our commercial paper program allows us to have a maximum of \$1,500 in commercial paper outstanding with maturities up to 397 days from the date of issuance. On March 31, 2019 there were no amounts outstanding under our commercial paper program.

We have lines of credit issued by various financial institutions that are available to fund our day-to-day operating needs. Certain of our credit facilities require us to comply with financial and other covenants. We were in compliance with all covenants on March 31, 2019.

| Summary of Total Debt | March<br>2019 | December<br>2018 |
|-----------------------|---------------|------------------|
|-----------------------|---------------|------------------|

## Senior unsecured notes:

| Rate                            | Due               |         |          |
|---------------------------------|-------------------|---------|----------|
| 1.800%                          | January 15, 2019  | \$—     | \$ 500   |
| 2.000%                          | March 8, 2019     | —       | 750      |
| 4.375%                          | January 15, 2020  | 499     | 499      |
| Variable                        | November 30, 2020 | 338     | 343      |
| 2.625%                          | March 15, 2021    | 748     | 747      |
| 1.125%                          | November 30, 2023 | 618     | 627      |
| 3.375%                          | May 15, 2024      | 585     | 584      |
| 3.375%                          | November 1, 2025  | 746     | 746      |
| 3.500%                          | March 15, 2026    | 990     | 990      |
| 2.125%                          | November 30, 2027 | 840     | 853      |
| 3.650%                          | March 7, 2028     | 595     | 595      |
| 2.625%                          | November 30, 2030 | 722     | 733      |
| 4.100%                          | April 1, 2043     | 391     | 391      |
| 4.375%                          | May 15, 2044      | 395     | 395      |
| 4.625%                          | March 15, 2046    | 980     | 980      |
| Other                           |                   | 24      | 126      |
| Total debt                      |                   | \$8,471 | \$ 9,859 |
| Less current maturities of debt |                   | 521     | 1,373    |
| Total long-term debt            |                   | \$7,950 | \$ 8,486 |

|                                      |         |          |
|--------------------------------------|---------|----------|
| Unamortized debt issuance costs      | \$48    | \$ 50    |
| Available borrowing capacity         | \$1,562 | \$ 1,548 |
| Fair value of senior unsecured notes | \$8,855 | \$ 9,746 |

The fair value of the senior unsecured notes was estimated using quoted interest rates, maturities and amounts of borrowings based on quoted active market prices and yields that took into account the underlying terms of the debt instruments. Substantially all our debt is classified within Level 2 of the fair value hierarchy.

## NOTE 9 - INCOME TAXES

Our effective tax rates were 14.2% and 18.3% in the three months 2019 and 2018. The decrease in the effective tax rate was primarily due to excess tax benefit from stock option exercises.

## NOTE 10 - SEGMENT INFORMATION

|              | Three Months |         |
|--------------|--------------|---------|
|              | 2019         | 2018    |
| Orthopaedics | \$1,250      | \$1,216 |

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|   |         |         |
|---|---------|---------|
| MedSurg                                     | 1,544   | 1,427   |
| Neurotechnology and Spine                   | 722     | 598     |
| Net sales                                   | \$3,516 | \$3,241 |
| Orthopaedics                                | \$437   | \$429   |
| MedSurg                                     | 377     | 301     |
| Neurotechnology and Spine                   | 199     | 178     |
| Segment operating income                    | \$1,013 | \$908   |
| Items not allocated to segments:            |         |         |
| Corporate and other                         | (132    | )(99 )  |
| Acquisition and integration-related charges | (138    | )(17 )  |
| Amortization of intangible assets           | (114    | )(102 ) |
| Restructuring-related charges               | (56     | )(63 )  |
| Medical device regulations                  | (7      | )—      |
| Recall-related matters                      | (13     | )(4 )   |
| Regulatory and legal matters                | (25     | )(32 )  |
| Consolidated operating income               | \$528   | \$591   |

There were no significant changes to total assets by segment from information provided in our Annual Report on Form 10-K for 2018.

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## STRYKER CORPORATION 2019 First Quarter Form 10-Q

## ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

## ABOUT STRYKER

Stryker Corporation ("we" or "our") is one of the world's leading medical technology companies and, together with our customers, we are driven to make healthcare better. We offer innovative products and services in Orthopaedics, Medical and Surgical, and Neurotechnology and Spine that help improve patient and hospital outcomes.

We segregate our operations into three reportable business segments: Orthopaedics, MedSurg, and Neurotechnology and Spine. Orthopaedics products consist primarily of implants used in hip and knee joint replacements and trauma and extremities surgeries. MedSurg products include surgical equipment and surgical navigation systems (Instruments), endoscopic and communications systems (Endoscopy), patient handling, emergency medical equipment and intensive care disposable products (Medical), reprocessed and remanufactured medical devices (Sustainability) and other medical device products used in a variety of medical specialties. Neurotechnology and Spine products include neurosurgical, neurovascular and spinal implant devices.

## Overview of the Three Months

In the three months 2019 we achieved sales growth of 8.5%. Excluding the impact of acquisitions sales grew 7.3% in constant currency. We reported operating income margin of 15.0%, net earnings of \$412 and net earnings per diluted share of \$1.09.

Excluding the impact of certain items, we expanded adjusted operating income margin 10 basis points to 25.1%, with adjusted net earnings<sup>(1)</sup> of \$714 and growth of 11.9% in adjusted net earnings per diluted share<sup>(1)</sup>.

## Recent Developments

In January 2019 we repaid \$500 of our senior unsecured notes with a coupon of 1.800% that were due on January 15, 2019. In March 2019 we repaid \$750 of our senior unsecured notes with a coupon of 2.000% that were due on March 8, 2019.

In the three months 2019 we completed two acquisitions for total cash consideration of \$180 with future milestone payments due upon the achievement of certain clinical and sales milestones.

In the three months 2019 we repurchased 1.9 million shares of our common stock at a cost of \$307 under our authorized repurchase program. The total dollar value of shares of our common stock that could be acquired under our authorized repurchase program was \$1,033 as of March 31, 2019.

On January 1, 2019 we adopted ASU 2016-02, Leases, and related amendments (ASC 842), which require lease assets and liabilities to be recorded on the balance sheet for leases with terms greater than twelve months. Refer to Note 6 for further information. The adoption of this update did not have a material impact on our Consolidated Financial Statements.

<sup>(1)</sup> Refer to "Non-GAAP Financial Measures" for a discussion of non-GAAP financial measures used in this report and a reconciliation to the most directly comparable GAAP financial measure.

## CONSOLIDATED RESULTS OF OPERATIONS

|  | Three Months |         | Percent Net Sales |         | Percentage |   |
|--|--------------|---------|-------------------|---------|------------|---|
|  | 2019         | 2018    | 2019              | 2018    | Change     | % |
| Net sales                                      | \$3,516      | \$3,241 | 100.0             | % 100.0 | % 8.5      | % |
| Gross profit                                   | 2,283        | 2,137   | 64.9              | 65.9    | 6.8        |   |
| Research, development and engineering expenses | 225          | 204     | 6.4               | 6.3     | 10.3       |   |
| Selling, general and administrative expenses   | 1,403        | 1,236   | 39.9              | 38.1    | 13.5       |   |
| Recall charges                                 | 13           | 4       | 0.4               | 0.1     | 225.0      |   |
| Amortization of intangible assets              | 114          | 102     | 3.2               | 3.1     | 11.8       |   |
| Other income (expense), net                    | (48)         | )(49)   | )(1.4             | ) (1.5  | ) (2.0     | ) |
| Income taxes                                   | 68           | 99      |                   |         | (31.3      | ) |

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|  |  |         |                   |        |      |       |        |    |
|--|--|---------|-------------------|--------|------|-------|--------|----|
| Net earnings   |  |         | \$412             | \$443  | 11.7 | %13.7 | %(7.0) | )% |
| Net earnings per diluted share                         |  |         | \$1.09            | \$1.16 |      |       | (6.0)  | )% |
| Adjusted net earnings per diluted share <sup>(1)</sup> |  |         | \$1.88            | \$1.68 |      |       | 11.9   | %  |
| Geographic and Segment Net Sales Three Months          |  |         |                   |        |      |       |        |    |
|  |  |         | Percentage Change |        |      |       |        |    |
|  |  |         | As Constant       |        |      |       |        |    |
|  |  |         | Reported Currency |        |      |       |        |    |
|  |  | 2019    | 2018              |        |      |       |        |    |
| Geographic:  |  |         |                   |        |      |       |        |    |
| United States  |  | \$2,579 | \$2,314           | 11.5   | %    | 11.5  | %      |    |
| International  |  | 937     | 927               | 1.1    |      | 8.3   |        |    |
| Total  |  | \$3,516 | \$3,241           | 8.5    | %    | 10.6  | %      |    |
| Segment:   |  |         |                   |        |      |       |        |    |
| Orthopaedics   |  | \$1,250 | \$1,216           | 2.8    | %    | 5.1   | %      |    |
| MedSurg  |  | 1,544   | 1,427             | 8.2    |      | 10.0  |        |    |
| Neurotechnology and Spine                              |  | 722     | 598               | 20.7   |      | 23.2  |        |    |
| Total  |  | \$3,516 | \$3,241           | 8.5    | %    | 10.6  | %      |    |

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## STRYKER CORPORATION 2019 First Quarter Form 10-Q

## Supplemental Net Sales Growth Information

|                                   | Three Months   |                | Percentage Change |                   |               |                   |              |                   |
|-----------------------------------|----------------|----------------|-------------------|-------------------|---------------|-------------------|--------------|-------------------|
|                                   | 2019           | 2018           | United States     |                   | International |                   | As Reported  | Constant Currency |
|                                   |                |                | As Reported       | Constant Currency | As Reported   | Constant Currency |              |                   |
| <b>Orthopaedics:</b>              |                |                |                   |                   |               |                   |              |                   |
| Knees                             | \$439          | \$419          | 4.9 %             | 7.0 %             | 6.6 %         | 0.5 %             | 8.1 %        | %                 |
| Hips                              | 336            | 331            | 1.5               | 4.1               | 4.0           | (2.4 )            | 4.4          |                   |
| Trauma and Extremities            | 396            | 389            | 1.7               | 4.1               | 3.4           | (1.2 )            | 5.4          |                   |
| Other                             | 79             | 77             | 2.1               | 3.5               | (0.3 )        | 12.5              | 21.4         |                   |
|                                   | \$1,250        | \$1,216        | 2.8 %             | 5.1 %             | 4.4 %         | (0.6 )            | 6.5 %        | %                 |
| <b>MedSurg:</b>                   |                |                |                   |                   |               |                   |              |                   |
| Instruments                       | \$478          | \$412          | 16.1 %            | 18.0 %            | 20.6 %        | 1.2 %             | 8.9 %        | %                 |
| Endoscopy                         | 470            | 444            | 5.7               | 7.5               | 7.5           | (1.0 )            | 7.5          |                   |
| Medical                           | 531            | 511            | 4.0               | 5.8               | 9.2           | (11.2 )           | (4.6 )       |                   |
| Sustainability                    | 65             | 60             | 9.0               | 9.0               | 8.4           | 117.6             | 128.2        |                   |
|                                   | \$1,544        | \$1,427        | 8.2 %             | 10.0 %            | 11.9 %        | (4.4 )            | 3.1 %        | %                 |
| <b>Neurotechnology and Spine:</b> |                |                |                   |                   |               |                   |              |                   |
| Neurotechnology                   | \$465          | \$410          | 13.6 %            | 16.1 %            | 16.0 %        | 9.5 %             | 16.2 %       | %                 |
| Spine                             | 257            | 188            | 36.3              | 38.6              | 40.9          | 23.6              | 32.0         |                   |
|                                   | \$722          | \$598          | 20.7 %            | 23.2 %            | 24.7 %        | 12.9 %            | 20.1 %       | %                 |
| <b>Total</b>                      | <b>\$3,516</b> | <b>\$3,241</b> | <b>8.5 %</b>      | <b>10.6 %</b>     | <b>11.5 %</b> | <b>1.1 %</b>      | <b>8.3 %</b> | <b>%</b>          |

## Consolidated Net Sales

Consolidated net sales increased 8.5% in the three months 2019 as reported and 10.6% in constant currency, as foreign currency exchange rates negatively impacted net sales by 2.1%. Excluding the 3.3% impact of acquisitions, net sales in constant currency increased by 8.7% from unit volume partially offset by 1.4% due to lower prices. The unit volume increase was primarily due to higher shipments of neurotechnology, instruments, knee, hip, medical and endoscopy products.

## Orthopaedics Net Sales

Orthopaedics net sales increased 2.8% in the three months 2019 as reported and 5.1% in constant currency, as foreign currency exchange rates negatively impacted net sales by 2.3%. Net sales in constant currency increased by 7.1% from unit volume partially offset by 2.1% due to lower prices. The unit volume increase was primarily due to higher shipments of knee, hip and trauma and extremities products.

## MedSurg Net Sales

MedSurg net sales increased 8.2% in the three months 2019 as reported and 10.0% in constant currency, as foreign currency exchange rates negatively impacted net sales by 1.8%. Excluding the 1.1% impact of acquisitions, net sales in constant currency increased by 9.9% from unit volume partially offset by 1.0% due to lower prices. The unit volume increase was primarily due to higher shipments of instruments, medical and endoscopy products.

## Neurotechnology and Spine Net Sales

Neurotechnology and Spine net sales increased 20.7% in the three months 2019 as reported and 23.2% in constant currency, as foreign currency exchange rates negatively impacted net sales by 2.5%. Excluding the 15.4% impact of acquisitions, net sales in constant currency increased by 8.9% from unit volume partially offset by 1.1% due to lower prices. The unit volume increase was primarily due to higher shipments of neurotechnology products.

## Gross Profit

Gross profit as a percentage of sales in the three months 2019 decreased to 64.9% from 65.9% in 2018. Excluding the impact of the items noted below, gross profit decreased to 65.8% of sales in the three months 2019 from 66.3% in

2018 primarily due to lower

selling prices and product mix, partially offset by increases due to leverage from higher sales volumes.

|   | Percent Net<br>Sales |         |       |       |
|---|----------------------|---------|-------|-------|
| Three Months                            | 2019                 | 2018    | 2019  | 2018  |
| Reported                                | \$2,283              | \$2,137 | 64.9% | 65.9% |
| Inventory stepped up to fair value      | 24                   | 6       | 0.7   | 0.2   |
| Restructuring-related and other charges | 5                    | 5       | 0.2   | 0.2   |
| Medical device regulations              | —                    | 1       | —     | —     |
| Adjusted                                | \$2,312              | \$2,149 | 65.8% | 66.3% |

#### Research, Development and Engineering Expenses

Research, development and engineering expenses increased \$21 or 10.3% to 6.4% of sales in the three months 2019 from 6.3% in 2018. Projects to develop new products, investments in new technologies and recent acquisitions contributed to the increased spending levels.

#### Selling, General and Administrative Expenses

Selling, general and administrative expenses increased \$167 or 13.5% in the three months 2019 and increased as a percentage of sales to 39.9% from 38.1% in 2018. Excluding the impact of the items noted below, expenses decreased to 34.5% of sales in 2019 from 35.0% in 2018, primarily due to leverage from higher sales volumes, continued focus on our operating expense improvement initiatives, partially offset by the leverage from recent acquisitions.

|   | Percent Net<br>Sales |         |       |       |
|---|----------------------|---------|-------|-------|
| Three Months                              | 2019                 | 2018    | 2019  | 2018  |
| Reported                                  | \$1,403              | \$1,236 | 39.9% | 38.1% |
| Other acquisition and integration-related | (114)                | (11)    | (3.2) | (0.3) |
| Restructuring-related and other charges   | (52)                 | (58)    | (1.5) | (1.8) |
| Regulatory and legal matters              | (25)                 | (32)    | (0.7) | (1.0) |
| Adjusted                                  | \$1,212              | \$1,135 | 34.5% | 35.0% |

#### Recall Charges

Recall charges were \$13 and \$4 in the three months 2019 and 2018. Charges were primarily due to the previously disclosed Rejuvenate and ABGII Modular-Neck hip stems and LFIT V40 femoral head voluntary recalls. Refer to Note 6 to our Consolidated Financial Statements for further information.

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## STRYKER CORPORATION 2019 First Quarter Form 10-Q

## Amortization of Intangible Assets

Amortization of intangible assets was \$114 and \$102 in the three months 2019 and 2018. The increase in 2019 was primarily due to our recent acquisitions. Refer to Note 7 to our Consolidated Financial Statements for further information.

## Operating Income

Operating Income decreased \$63 or 10.7% to 15.0% of net sales in the three months 2019 from 18.2% in 2018. Excluding the impact of the items noted below, operating income increased to 25.1% of sales in 2019 from 25.0% in 2018 primarily due to leverage from higher sales volumes, continued focus on our operating expense improvement initiatives, partially offset by lower selling prices.

| Three Months                                | Percent Net Sales |       |       |       |
|---|-------------------|-------|-------|-------|
|   | 2019              | 2018  | 2019  | 2018  |
| Reported                                    | \$528             | \$591 | 15.0% | 18.2% |
| Inventory stepped up to fair value          | 24                | 6     | 0.7   | 0.2   |
| Other acquisition and integration-related   | 114               | 11    | 3.2   | 0.4   |
| Amortization of purchased intangible assets | 114               | 102   | 3.2   | 3.2   |
| Restructuring-related and other charges     | 56                | 63    | 1.6   | 1.9   |
| Medical device regulations                  | 7                 | 1     | 0.2   | —     |
| Recall-related matters                      | 13                | 4     | 0.4   | 0.1   |
| Regulatory and legal matters                | 25                | 32    | 0.8   | 1.0   |
| Adjusted                                    | \$881             | \$810 | 25.1% | 25.0% |

## Other Income (Expense), Net

Other income (expense), net was (\$48) and (\$49) in the three months 2019 and 2018. The decrease in 2019 was primarily due to an increase in interest income due to higher interest rates partially offset by higher interest expense due to higher interest rates.

## Income Taxes

The effective tax rates were 14.2% and 18.3% in the three months 2019 and 2018. The decrease in the effective tax rate in 2019 was primarily due to excess tax benefit from stock option exercises.

## Net Earnings

Net earnings decreased to \$412 or \$1.09 per diluted share in the three months 2019 from \$443 or \$1.16 per diluted share in 2018. Adjusted net earnings per diluted share<sup>(1)</sup> increased 11.9% to \$1.88 in 2019 from \$1.68 in 2018. The impact of foreign currency exchange rates was to decrease net earnings per diluted share by approximately \$0.06 in 2019 and increase net earnings per diluted share by approximately \$0.02 in 2018.

| Three Months                                | Percent Net Sales |       |       |       |
|---|-------------------|-------|-------|-------|
|   | 2019              | 2018  | 2019  | 2018  |
| Reported                                    | \$412             | \$443 | 11.7% | 13.7% |
| Inventory stepped up to fair value          | 19                | 4     | 0.5   | 0.1   |
| Other acquisition and integration-related   | 88                | 9     | 2.5   | 0.3   |
| Amortization of purchased intangible assets | 91                | 83    | 2.6   | 2.6   |
| Restructuring-related and other charges     | 50                | 50    | 1.5   | 1.6   |
| Medical device regulations                  | 6                 | 1     | 0.2   | —     |
| Recall-related matters                      | 10                | 3     | 0.3   | 0.1   |
| Regulatory and legal matters                | 19                | 24    | 0.5   | 0.7   |
| Tax matters                                 | 19                | 21    | 0.5   | 0.6   |
| Adjusted                                    | \$714             | \$638 | 20.3% | 19.7% |

<sup>(1)</sup>Non-GAAP Financial Measures

We supplement the reporting of our financial information determined under accounting principles generally accepted in the United States (GAAP) with certain non-GAAP financial measures, including percentage sales growth in



constant currency; percentage organic sales growth; adjusted gross profit; adjusted selling, general and

administrative expenses; adjusted amortization of intangible assets; adjusted operating income; adjusted effective income tax rate; adjusted net earnings; and adjusted net earnings per diluted share (Diluted EPS). We believe these non-GAAP financial measures provide meaningful information to assist investors and shareholders in understanding our financial results and assessing our prospects for future performance. Management believes percentage sales growth in constant currency and the other adjusted measures described above are important indicators of our operations because they exclude items that may not be indicative of or are unrelated to our core operating results and provide a baseline for analyzing trends in our underlying businesses. Management uses these non-GAAP financial measures for reviewing the operating results of reportable business segments and analyzing potential future business trends in connection with our budget process and bases certain management incentive compensation on these non-GAAP financial measures. To measure percentage sales growth in constant currency, we remove the impact of changes in foreign currency exchange rates that affect the comparability and trend of sales. Percentage sales growth in constant currency is calculated by translating current and prior year results at the same foreign currency exchange rate. To measure percentage organic sales growth, we remove the impact of changes in foreign currency exchange rates and acquisitions, which affect the comparability and trend of sales. Percentage organic sales growth is calculated by translating current year results at prior year average foreign currency exchange rates excluding the impact of acquisitions. To measure earnings performance on a consistent and comparable basis, we exclude certain items that affect the comparability of operating results and the trend of earnings. These adjustments are irregular in timing and may not be indicative of our past and future performance. The following are examples of the types of adjustments that may be included in a period:

1. Acquisition and integration-related costs. Costs related to integrating recently acquired businesses and specific costs (e.g., inventory step-up and deal costs) related to the consummation of the acquisition process.
2. Amortization of purchased intangible assets. Periodic amortization expense related to purchased intangible assets.
3. Restructuring-related and other charges. Costs associated with the termination of sales relationships in certain countries, workforce reductions, elimination of product lines, weather-related asset impairments and associated costs and other restructuring-related activities.
4. Medical Device Regulations. Costs specific to updating our quality system, product labeling, asset write-offs and product remanufacturing to comply with the medical device reporting regulations and other requirements of the European Union and China regulations for medical devices.
5. Recall-related matters. Our best estimate of the minimum of the range of probable loss to resolve the Rejuvenate, LFIT V40 and other product recalls.
6. Regulatory and legal matters. Our best estimate of the minimum of the range of probable loss to resolve certain regulatory matters and other legal settlements.
7. Tax matters. Charges represent the impact of accounting for certain significant and discrete tax items.

Because non-GAAP financial measures are not standardized, it may not be possible to compare these financial measures with other companies' non-GAAP financial measures having the same or similar names. These adjusted financial measures should not be considered in isolation or as a substitute for reported sales growth, gross profit, selling, general and administrative expenses, amortization of intangible assets, operating income, effective

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## STRYKER CORPORATION 2019 First Quarter Form 10-Q

income tax rate, net earnings and net earnings per diluted share, the most directly comparable GAAP financial measures. These non-GAAP financial measures are an additional way of viewing aspects of our operations when viewed with our GAAP results and the reconciliations to corresponding GAAP financial measures at the end of the discussion of Consolidated Results of Operations below. We strongly encourage investors and shareholders to review our financial statements and publicly-filed reports in their entirety and not to rely on any single financial measure.

The weighted-average diluted shares outstanding used in the calculation of non-GAAP net earnings per diluted share are the same as those used in the calculation of reported net earnings per diluted share for the respective period.

## Reconciliation of Non-GAAP Financial Measures to the Most Directly Comparable GAAP Financial Measures

| Three Months 2019                            | Gross Profit | Selling, General & Administrative Expenses | Amortization of Intangible Assets | Operating Income | Net Earnings | Effective Tax Rate | Diluted EPS |
|--|--------------|--|-----------------------------------|------------------|--------------|--------------------|-------------|
| Reported                                     | \$2,283      | \$ 1,403                                   | \$ 114                            | \$ 528           | \$ 412       | 14.2 %             | \$ 1.09     |
| Reported percent net sales                   | 64.9 %       | 39.9 %                                     | 3.2 %                             | 15.0 %           | 11.7 %       |                    |             |
| Acquisition and integration-related charges: |              |  |                                   |                  |              |                    |             |
| Inventory stepped up to fair value           | 24           | —  | —                                 | 24               | 19           | 0.3                | 0.05        |
| Other acquisition and integration-related    | —            | (114)                                      | —                                 | 114              | 88           | 2.0                | 0.23        |
| Amortization of purchased intangible assets  | —            | —  | (114)                             | 114              | 91           | 1.3                | 0.24        |
| Restructuring-related and other charges      | 5            | (52)                                       | —                                 | 56               | 50           | (0.3)              | 0.13        |
| Medical device regulations                   | —            | —  | —                                 | 7                | 6            | 0.1                | 0.01        |
| Recall-related matters                       | —            | —  | —                                 | 13               | 10           | 0.3                | 0.03        |
| Regulatory and legal matters                 | —            | (25)                                       | —                                 | 25               | 19           | 0.4                | 0.05        |
| Tax matters                                  | —            | —  | —                                 | —                | 19           | (3.9)              | 0.05        |
| Adjusted                                     | \$2,312      | \$ 1,212                                   | \$ —                              | \$ 881           | \$ 714       | 14.4 %             | \$ 1.88     |
| Adjusted percent net sales                   | 65.8 %       | 34.5 %                                     | — %                               | 25.1 %           | 20.3 %       |                    |             |
| Three Months 2018                            | Gross Profit | Selling, General & Administrative Expenses | Amortization of Intangible Assets | Operating Income | Net Earnings | Effective Tax Rate | Diluted EPS |
| Reported                                     | \$2,137      | \$ 1,236                                   | \$ 102                            | \$ 591           | \$ 443       | 18.3 %             | \$ 1.16     |
| Reported percent net sales                   | 65.9 %       | 38.1 %                                     | 3.1 %                             | 18.2 %           | 13.7 %       |                    |             |
| Acquisition and integration-related charges: |              |  |                                   |                  |              |                    |             |
| Inventory stepped up to fair value           | 6            | —  | —                                 | 6                | 4            | 0.2                | 0.01        |
| Other acquisition and integration-related    | —            | (11)                                       | —                                 | 11               | 9            | —                  | 0.02        |
| Amortization of purchased intangible assets  | —            | —  | (102)                             | 102              | 83           | 0.4                | 0.22        |
| Restructuring-related and other charges      | 5            | (58)                                       | —                                 | 63               | 50           | 0.5                | 0.13        |
| Medical device regulations                   | 1            | —  | —                                 | 1                | 1            | —                  | —           |
| Recall-related matters                       | —            | —  | —                                 | 4                | 3            | 0.1                | 0.01        |
| Regulatory and legal matters                 | —            | (32)                                       | —                                 | 32               | 24           | 0.5                | 0.07        |
| Tax matters                                  | —            | —  | —                                 | —                | 21           | (3.9)              | 0.06        |
| Adjusted                                     | \$2,149      | \$ 1,135                                   | \$ —                              | \$ 810           | \$ 638       | 16.1 %             | \$ 1.68     |
| Adjusted percent net sales                   | 66.3 %       | 35.0 %                                     | — %                               | 25.0 %           | 19.7 %       |                    |             |

## FINANCIAL CONDITION AND LIQUIDITY

Three Months 2019    2018

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|  |           |         |
|--|-----------|---------|
| Net cash provided by operating activities                    | \$313     | \$297   |
| Net cash used in investing activities                        | (303)     | (849)   |
| Net cash (used in) provided by financing activities          | (1,947)   | 145     |
| Effect of exchange rate changes on cash and cash equivalents | (5)       | 44      |
| Change in cash and cash equivalents                          | \$(1,942) | \$(363) |

Operating Activities

Cash provided by operating activities was \$313 and \$297 in the three months 2019 and 2018. The increase was primarily due to the receipt of cash related to a prospective legal settlement partially offset by lower earnings. Refer to Note 6 to our Consolidated Financial Statements for further information.

Investing Activities

Cash used in investing activities was \$303 and \$849 in the three months 2019 and 2018. The decrease in cash used was primarily due to decreased payments for acquisitions in 2019.

Financing Activities

Cash (used in) provided by financing activities was (\$1,947) and \$145 in the three months 2019 and 2018. The increase in cash used was primarily driven by the repayment of \$1,341 of debt upon maturity in 2019, \$307 of repurchases of common stock and \$195 of dividend payments.

| Three Months                                     | 2019  | 2018  |
|--|-------|-------|
| Total dividends paid to common shareholders      | \$195 | \$176 |
| Total amount paid to repurchase common stock     | \$307 | \$300 |
| Shares of repurchased common stock (in millions) | 1.9   | 1.9   |

Liquidity

Cash, cash equivalents and marketable securities were \$1,758 and \$3,699 on March 31, 2019 and December 31, 2018. Current assets exceeded current liabilities by \$4,175 and \$4,926 on March 31, 2019 and December 31, 2018. We anticipate being able to support our short-term liquidity and operating needs from a variety of sources including cash from operations, commercial paper and existing credit lines. We raised funds in the capital markets in 2018

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STRYKER CORPORATION 2019 First Quarter Form 10-Q

and may continue to do so from time to time. We continue to have strong investment-grade short-term and long-term debt ratings that we believe should enable us to refinance our debt as needed.

Our cash, cash equivalents and marketable securities held in locations outside the United States was approximately 47% on March 31, 2019 compared to 25% on December 31, 2018. We intend to use this cash to expand operations organically and through acquisitions.

**Critical Accounting Policies**

There were no changes to our critical accounting policies from those disclosed in our Annual Report on Form 10-K for 2018.

**New Accounting Pronouncements Not Yet Adopted**

Refer to Note 1 to our Consolidated Financial Statements for information.

**Guarantees and Other Off-Balance Sheet Arrangements**

We do not have guarantees or other off-balance sheet financing arrangements, including variable interest entities, of a magnitude that we believe could have a material impact on our financial condition or liquidity.

**OTHER MATTERS**

**Legal and Regulatory Matters**

We are involved in various ongoing proceedings, legal actions and claims arising in the normal course of our business, including proceedings related to product, labor, intellectual property and other matters. Refer to Note 6 to our Consolidated Financial Statements for further information.

**FORWARD-LOOKING STATEMENTS**

This report contains statements referring to us that are not historical facts and are considered "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995. These statements, which are intended to take advantage of the "safe harbor" provisions of the Reform Act, are based on current projections about operations, industry conditions, financial condition and liquidity. Words that identify forward-looking statements include words such as "may," "could," "will," "should," "possible," "plan," "predict," "forecast," "potential," "anticipate," "estimate," "expect," "project," "intend," "believe," "may impact," "on track," "goal," "strategy" and words and terms of similar substance used in connection with any discussion of future operating or financial performance, an acquisition or our businesses. In addition, any statements that refer to expectations, projections or other characterizations of future events or circumstances, including any underlying assumptions, are forward-looking statements. Those statements are not guarantees and are subject to risks, uncertainties and assumptions that are difficult to predict. Therefore, actual results could differ materially and adversely from these forward-looking statements. Some important factors that could cause our actual results to differ from our expectations in any forward-looking statements include those risks discussed in Item 1A. "Risk Factors" of our Annual Report on Form 10-K for 2018. This Form 10-Q should be read in conjunction with our Consolidated Financial Statements and accompanying notes to our Consolidated Financial Statements in our Annual Report on Form 10-K for 2018.

**ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

We consider our greatest potential area of market risk exposure to be exchange rate risk. Quantitative and qualitative disclosures about exchange rate risk are included in Item 7A "Quantitative and Qualitative Disclosures About Market Risk" of our Annual Report on Form 10-K for 2018. There were no material changes from the

information provided therein.

**ITEM 4. CONTROLS AND PROCEDURES**

**Evaluation of Disclosure Controls and Procedures**

Our management, with the participation of the Chief Executive Officer and Chief Financial Officer (the Certifying Officers), evaluated the effectiveness of the Company's disclosure controls and procedures (as defined in Rules 13a-15(e) or 15d-15(e) promulgated under the Securities Exchange Act of 1934, as amended) on March 31, 2019. Based on that evaluation, the Certifying Officers concluded the Company's disclosure controls and procedures were effective as of March 31, 2019.

**Changes in Internal Control Over Financial Reporting**

There was no change to our internal control over financial reporting during the three months 2019 that materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

## PART II – OTHER INFORMATION

### ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

We issued 6,779 shares of our common stock in the three months 2019 as performance incentive awards to employees. These shares were not registered under the Securities Act of 1933 based on the conclusion that the awards would not be events of sale within the meaning of Section 2(a)(3) of the Act.

In March 2015 we announced that our Board of Directors had authorized us to purchase up to \$2,000 of our common stock. The manner, timing and amount of repurchases are determined by management based on an evaluation of market conditions, stock price, and other factors and are subject to regulatory considerations. Purchases are made from time to time in the open market, in privately negotiated transactions or otherwise.

In 2019 we repurchased 1.9 million shares of our common stock at a cost of \$307 under our authorized repurchase program. The total dollar value of shares of our common stock that could be acquired under our authorized repurchase program was \$1,033 as of March 31, 2019.

| 2019 Period | Total Number of<br>Shares<br>(in millions) |  | Average<br>Price<br>Paid<br>Per<br>Share | Approximate<br>Dollar Value<br>of Shares that may<br>yet be Purchased<br>Under the Plans |
|-------------|--|--|--|--|
|             | Total<br>Purchased                         | Part of<br>Public<br>Share<br>Announced<br>Purchase<br>Plans |  |  |
| January     | 1.9  | 1.9  | \$161.35                                 | \$ 1,033   |
| February    | —  | —  | —  | 1,033  |
| March       | —  | —  | —  | \$ 1,033   |
| Total       | 1.9  | 1.9  | \$161.35                                 |  |

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STRYKER CORPORATION 2019 First Quarter Form 10-Q

ITEM 6. EXHIBITS

- 10(i) Transition and Retention Agreement between Stryker Corporation and Michael Hutchinson, dated March 25, 2019 - Incorporated by reference to Exhibit 10.1 to the Company's Form 8-K dated March 27, 2019 (Commission File No. 001-13149)
- 31(i)\* Certification of Principal Executive Officer of Stryker Corporation pursuant to Rule 13a-14(a)
- 31(ii)\* Certification of Principal Financial Officer of Stryker Corporation pursuant to Rule 13a-14(a)
- 32(i)\* Certification by Principal Executive Officer of Stryker Corporation pursuant to 18 U.S.C. Section 1350
- 32(ii)\* Certification by Principal Financial Officer of Stryker Corporation pursuant to 18 U.S.C. Section 1350
- 101.INS XBRL Instance Document
- 101.SCH XBRL Schema Document
- 101.CAL XBRL Calculation Linkbase Document
- 101.DEF XBRL Definition Linkbase Document
- 101.LAB XBRL Label Linkbase Document
- 101.PRE XBRL Presentation Linkbase Document
- † Filed with this Form 10-Q
- \* Furnished with this Form 10-Q

STRYKER CORPORATION 2019 First Quarter Form 10-Q

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

STRYKER CORPORATION  
(Registrant)

Date: April 24, 2019 /s/ KEVIN A. LOBO  
Kevin A. Lobo  
Chairman and Chief Executive Officer

Date: April 24, 2019 /s/ GLENN S. BOEHNLEIN  
Glenn S. Boehnlein  
Vice President, Chief Financial Officer