STRYKER CORP
Form 10-Q
April 24, 2019

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

FORM 10-Q

[X] 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, Michigan	49002
(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 [X] 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 [X] 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	[X]	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. [ ]

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). YES [ ] NO [X]
There were 373,810,085 shares of Common Stock, $0.10 par value, on March 31, 2019.

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.

STRYKER CORPORATION 2019 First Quarter Form 10-Q

CONSOLIDATED BALANCE SHEETS

	March 31	December 31
	2019	2018
	(Unaudited)	
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

CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY (Unaudited)

	Three Months 2019		Three Months 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

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.

Dollar amounts are in millions except per share amounts or as otherwise specified. 4

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

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.

Dollar amounts are in millions except per share amounts or as otherwise specified. 5

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

Three Months 2019	Marketable Securities	Pension Plans	Hedges	Financial Statement 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 Securities	Pension Plans	Hedges	Financial Statement 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	—	—	—

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

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

Fair Value of Available for Sale Securities by Maturity

	March 2019	December 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

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.

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 2019
Right-of-use assets	$ 355
Lease liabilities, current	89
Lease liabilities, non-current	258
Other information	
Weighted-average remaining lease term	5.5 years
Weighted-average discount rate	3.63 %

	Three Months 2019
Operating lease cost	$ 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

	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 2019	2020	2021	2022	2023
$333	$422	$409	$401	$381

Dollar amounts are in millions except per share amounts or as otherwise specified. 8

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 2019	December 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

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.

Dollar amounts are in millions except per share amounts or as otherwise specified. 9

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(1) of $714 and growth of 11.9% in adjusted net earnings per diluted share(1).

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.

(1) 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			