

## Perspective

### [Stryker: A Look Behind the Numbers](#)

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*Stryker Corp. has been proactive in positioning itself for success.*

One of the most active deal-makers in the medical device space and with a war chest of \$4 billion in cash, Stryker has demonstrated boldness and foresight in its recent acquisitions of Trauson and MAKO and, more recently, Patient Safety Technologies, Berchtold and Pivot Medical under the helm of new CEO, Kevin Lobo.

Stryker Corporation (SYK) seems to be poised for continued sales success in 2014. The Corporation continues to strategically leverage its strong balance sheet, its expansive global distribution network and its deep product portfolio to drive accelerated growth. The Orthopedics Division continues to grow at above-market rates, taking share in the hip and extremities markets, and maintaining its position in knees -- despite competitive knee launches during 2012 by Zimmer and DePuy Synthes. The sales trend is expected to continue through 2014.

The future direction the healthcare giant will pursue was revealed at Stryker's Analyst Meeting in September and during the Quarter 4, 2013 Earnings Call in January. Summarized below (in Q&A format) are: the Corporation's "Strategic Themes", the Orthopedic Division's "Primary Objectives", the latest Developments at the Stryker International Division and the Corporation's most recent M&A activities.

#### **1. Question: What Were the "Four Strategic Themes" Discussed by SYK Leadership?**

**Answer: Globalization, innovation, collaboration and cost optimization.**

- Globalization – Corporation sees a significant opportunity to grow the premium-price segment of outside-US markets and the lower price segment through the Trauson (China) acquisition
- Innovation – SYK seeks to expand innovation beyond products to the "entire procedure" and through customer education

- Collaboration – CEO is encouraging the Divisions to work together to leverage the breadth of SYK’s entire product portfolio with its customers
- Cost Optimization – Corporation is targeting an annual 3 to 5% reduction in cost of goods

**2. Question: What Were the Two Primary Objectives of Each SYK Division – Including Orthopedics?**

**Answer: Driving growth and delivering leverage.**

*Driving Growth*

A) Growing Sales

- US field sales force is ~2,500 strong
- About 1,900 are specialized either in: Recon, Trauma, or Foot & Ankle (initiated in early 2012), or Spine – balance are “full-line” reps
- Division is committed to increasing sales force specialization

B) Expanding And Diversifying Product Portfolio

- Ortho is focused on simplification and diversification
- Simplification, as viewed by the surgeon and hospital, will revolve around:
  - Making the procedure easier, more efficient, and less invasive;
  - Reducing procedural steps and instruments; and
  - Removing cost
- Differentiation will center on:
  - Seeking new segments that SYK can develop; and,
  - Introducing differentiated, new products in new markets
- Portfolio expansion will most likely occur in extremities (especially foot & ankle), and the minimally invasive and novel interbody sub-segments of spine
  - A reverse shoulder, FDA cleared in December, will be released in Q2/14 with full launch expected in Q3/14
  - “Most significant gaps in extremities (portfolio) are upper extremities – small joints, fingers, wrist, and elbow”
  - The Company may add a total ankle – probably the most significant gap in SYK’s lower extremity portfolio – but wants to first ensure it’s a “really compelling product”
  - Significant lower extremities growth in 2013 “is about market expansion and getting (foot & ankle) products into the hands of new physicians that were not using implants.....including podiatrists”



### C) Broadening the Capabilities of Biologics

- The Orthopedics Division plans to build on Orthovita's competencies, including: R&D, clinical and regulatory, manufacturing (collagen processing technology), and marketing

### D) Collaborating on a Cross-Divisional Basis and across the Product Portfolio

- Orthopedics seeks to exploit the power in portfolio breadth and depth – across all SYK Divisions

### *Delivering Leverage*

A) Division is focusing on power brands with “Proven Designs Refined” tag-line, including:

- Accolade II Hip, which builds on a decade-plus heritage of the original design;
- Secur-Fit Advanced Hip, where an internal database was used to modernize the femoral stem component; and
- Triathlon Knee, which has been expanded with all-poly tibial components and titanium base plates – with additional opportunities identified on the instrument side

### B) Tapping the Capabilities of Biologics

- Ortho is considering bringing distributed products in-house to “capture the margin”

### C) Improving Inventory Management

- Division plans to increase efficiencies and reduce costs related to product movement and tracking
- RFID tracking (chips on implants) program has been implemented
- SYK Corp's inventory days were 152 in Q4/14, down 33 days from Q4/12

### **3. Question: What Are The Latest Developments At Stryker International?**

**Answers: Stryker is seeking to increase current emerging market sales, which comprised 7% of total Corporation sales in 2013, into double-digit range. Priority countries include China, India, Brazil, Russia and Turkey.**

- About 35% of the Corporation's 2013 sales were outside the US; only 7% were in emerging markets
- SYK's annual emerging market growth has been “in the 20% range”. As a comparison, “most device companies have secured growth between 20 to 40% per annum”. The Corporation will look to “move closer to 40% annual growth and take 6% (in 2012) of

emerging market sales into double-digit range”. Note: SYK’s sales from emerging markets was 7% of total sales in 2013 and is projected to be 8% in 2014.

- Stryker has moved to a geographic alignment, including the America’s; Western Europe; Eastern Europe, Middle East and Africa (including “priority countries” of Russia and Turkey); Asia Pacific (including “priority countries” of China and India); and Japan
- Latest developments in Europe include:
  - New leadership,
  - Focus on increasing market share and improving margins,
  - Placing centralized marketing resources back in countries,
  - Redeploying resources between Southern and Northern Europe,
  - Optimizing distribution channels, and
  - Improving performance in Germany and addressing challenges in Italy
- Latest developments in Emerging Markets include:
  - Identifying “must-win markets” – China, India, Brazil, Russia and Turkey
  - In China, Trauson is providing products for the low-cost segment (Trauson products will be launched in other emerging markets as well) and sales reps are being added,
  - In India, a big investment has been made in a technical center
  - In Russia, significant distribution capacity has been added
  - In Turkey, distribution models are being optimized to ensure selection of the right partners

#### **4. Question: What Is The Latest Re: Stryker’s M&A Activities?**

**Answers: Acquisitions are the # 1 priority for the ~\$4 billion in cash (and equivalents) on SYK’s Balance Sheet. Although the Corporation has offered little information on the recent MAKO and Patient Safety Technologies transactions – it did announce 2 new acquisitions (Berchtold and Pivot Medical) in February.**

#### **MAKO**

- Acquisition closed in December, 2013
  - SYK “did the deal because we believe it is potentially transformational on orthopedic surgery and will allow Company to drive meaningful share gains”
  - “Analysis suggests a bigger opportunity in total hips and total knees to leverage SYK’s reconstructive implants”
  - Company currently has “close to 20% market share in the uni knee segment”
- Robotics One Of Several Available Solutions
  - SYK will offer “solutions for every surgeon preference”, whether standard instruments, (patient-specific) cutting blocks, navigation or robotics

- Short Term focus for robotics includes:
  - “Leveraging SYK’s considerable sales and distribution capabilities to help drive adoption for current applications”,
  - “Enabling SYK-marketed implants to be put on robot software”, and
  - “Starting the trial for a total knee application....in first half of the year”
  - In addition, per SYK: “It’s a little early for bi-cruciate (knee).....(and we will need) to determine whether it’s more than just a niche”
- Longer Term focus for robotics:
  - “By allowing for bone preparation and geometry and precision not possible with conventional manual instrumentation, there’s a potential to develop new implant designs that specifically enable robotics capability and functionality”, and
  - Expanding MAKO sales outside the US
- Other
  - Capital equipment will continue to be sold by the MAKO sales force, not the SYK capital equipment team – and remain separate from Navigation

### ***Patient Safety Technologies (PST)***

- Acquisition was announced on 12.31.13 and is expected to close by the end of Q1/14
- SYK acquired Company for \$120 million; PST’s sales thru the first nine months of 2013 were \$14.9 million (~ \$21 million annualized)
- PST has established a “strong customer base of over 300 hospitals”
- Per SYK: “PST’s portfolio aligns with the SYK Instruments Division (which is) focused on customer solutions that enhance patient and caregiver safety”
  - PST’s Safety-Sponge System “helps prevent retained foreign objects (RFO’s) in the OR, improving patient safety and reducing healthcare costs”
  - “The System includes bar-coded surgical sponges and towels, integrated barcode scanner and compliance tracking software”
  - “2,300 RFO’s are reported annually at an average cost per incident of over \$400,000”

### ***Berchtold Holdings, AG***

- Acquisition was announced on February 18th and expected to close by end Q1/14
- SYK acquired Berchtold for an enterprise value of \$172 million; Berchtold’s 2013 revenues were estimated at \$125 million.
- Berchtold, a privately held business with operating facilities in Germany and the United States, sells surgical infrastructure equipment

- Their product portfolio includes surgical tables, equipment booms, and surgical lighting systems geared towards maximizing efficiency and safety in operating rooms and ICUs
- Combining the Berchtold products with Stryker Endoscopy's existing operating room equipment portfolio will create a more comprehensive offering equipped to satisfy a wider range of customers
- Per SYK, "We are committed to offering innovative, best-in-class operating room infrastructure equipment. This acquisition delivers on that commitment by strengthening our portfolio and allowing us to address rapidly evolving customer requirements for operating room design."

### ***Pivot Medical, Inc.***

- Acquisition was announced on February 19th and is expected to close by end of March
- Pivot is a privately held business selling innovative products for hip arthroscopy with operating facilities in Sunnyvale, CA.
- Approximately \$40 million of VC monies had been invested in Company
- Pivot has a platform of instruments and implants to efficiently access and restore the mobility of the hip with minimal incisions.
- Hip arthroscopy is the fastest growing procedure in Sports Medicine resulting from improved procedural solutions and growing demand for less invasive solutions
- Per SYK, "This acquisition will allow us to combine Pivot's innovative platforms in hip arthroscopy with Stryker's knee and shoulder Sports Medicine solutions, and full line of arthroscopy visualization and tissue resection devices."

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