INNOVATION FOR A WORLD IN MOTION

Stryker Corporation 2002 Annual Report

CONTENTS

Company Overview

Stryker Corporation develops, manufactures and markets specialty surgical and medical products worldwide. These products include reconstructive implants; spinal, trauma and craniomaxillofacial (CMF) systems; the bone growth factor osteogenic protein-1; powered surgical instruments; endoscopic and surgical navigation systems; and patient care and handling equipment. The Company also provides out-patient rehabilitative health services in the United States.

Stryker Divisions

ORTHOPAEDIC IMPLANTS

Reconstructive Implants

Stryker Howmedica Osteonics
Orthopaedic reconstructive products including hip, knee and shoulder implants and bone cement. Production facilities in New Jersey, Ireland and France.

Spinal Systems

Stryker Spine
Spinal implant products including cervical, thoracolumbar and interbody systems used in spine injury, deformity and degenerative therapies. Global development centers in New Jersey and France; production facilities in France.

Trauma and CMF Systems

Stryker Trauma
Trauma-related products including nailing, plating and external fixation systems. Production facilities in Germany and Switzerland.

Stryker Leibinger
Plating systems and related products for craniomaxillofacial surgery; surgical navigation systems. Production facilities in Michigan and Germany.

Biotechnology

Stryker Biotech
Osteogenic protein-1 (OP-1) bone growth factor. Production facilities in Massachusetts, New Hampshire and Ireland.

Financial Highlights

(in millions, except per share amounts)

	2002	2001	% Change
Net sales	$3,011.6	$2,602.3	16
Earnings before income taxes and extraordinary item	506.7	405.7	25
Income taxes	161.1	133.9	20
Earnings before extraordinary item	345.6	271.8	27
Extraordinary loss, net of income taxes	–	(4.8)	–
Net earnings	$345.6	$267.0	29
Diluted earnings per share of common stock:			
Before extraordinary item	$1.70	$1.34	27
Extraordinary loss	–	($.02)	–
Net earnings	$1.70	$1.32	29

MEDICAL AND SURGICAL EQUIPMENT

Stryker Instruments
Powered surgical instruments, operating room equipment and interventional pain products. Production facilities in Michigan, Puerto Rico and Ireland.

Stryker Endoscopy
Medical video-imaging and communications equipment and instruments for arthroscopy and general surgery. Production facilities in California and Puerto Rico.

Stryker Medical
Specialty hospital beds and stretchers, general patient-room beds and emergency medical service products. Production facilities in Michigan and Canada.

REHABILITATIVE MEDICAL SERVICES

Physiotherapy Associates
Outpatient rehabilitation services focusing on physical and occupational therapy; 331 locations throughout the United States.

INTERNATIONAL SALES

Stryker Europe
Sale and distribution of Stryker products throughout Europe, the Middle East and Africa.

Stryker Japan
Sale and distribution of Stryker products in Japan.

Stryker Pacific
Sale and distribution of Stryker products throughout Asia and the Pacific, with the exception of Japan.

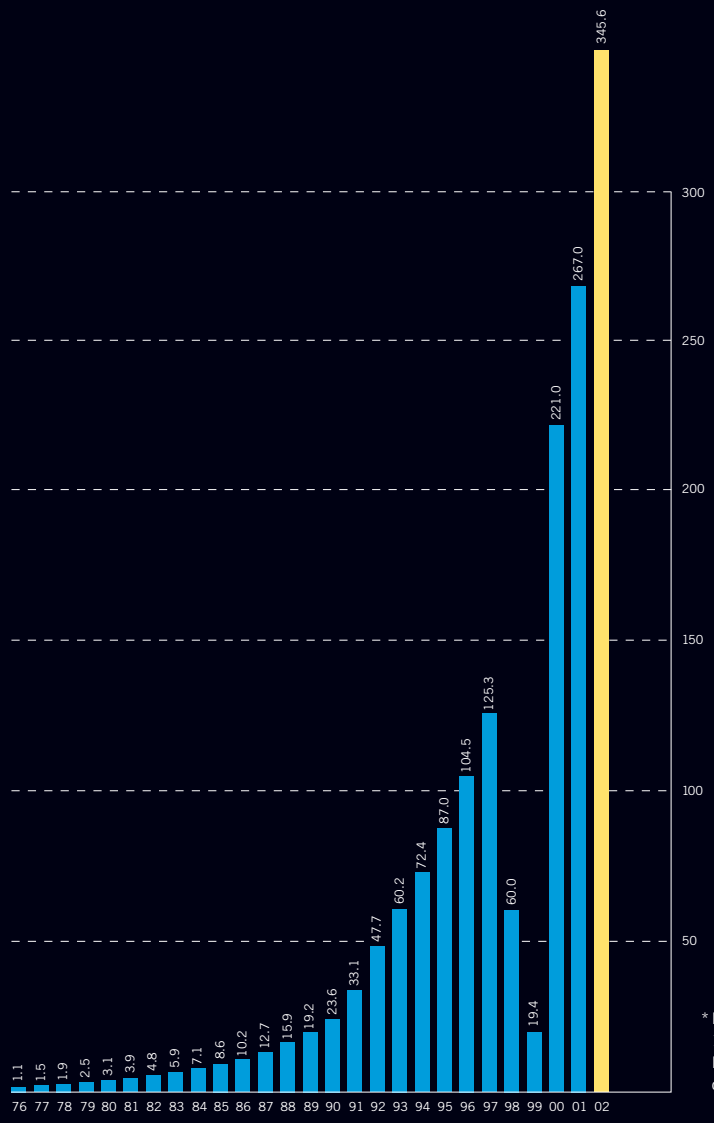
Stryker Canada
Sale and distribution of Stryker products in Canada.

Stryker Latin America
Sale and distribution of Stryker products throughout Central and South America, Mexico and the Caribbean.

In a world of rapid change, Stryker's continuing mission is to serve patients, surgeons and health-care systems around the world with best-in-class surgical and medical products. We have dedicated ourselves to this purpose by developing, manufacturing and marketing products aimed at emerging needs. Today, through exacting planning and execution, we are delivering on our commitment as demographic trends around the globe hold the promise of sustained high demand for our products. We are proud that our strategic decisions and execution are benefiting our customers, patients, employees and shareholders.

STRYKER INNOVATES TO MAKE A DIFFERENCE.

NET EARNINGS*
($ millions)
26-Year Compound Annual
Growth Rate of 25%



* Before 1990 extraordinary gain; 1998 and 1999 reflect Howmedica acquisition-related costs and charges.

To Our Shareholders:

It is gratifying to report to you on Stryker's progress in 2002. The year was highly successful, marked by robust sales of new and established products, initiatives to drive innovation for the future, strong leadership across the management team and excellent financial performance. Never has the Company been so ready to compete effectively in the worldwide orthopaedic marketplace, and never has that marketplace needed our products more. Around the globe, aging populations and lifestyle changes have created unprecedented and escalating demand for the products we invent, make and sell. While we have enjoyed much success in the past, the future holds even more opportunity for us to capitalize on our leading products, sales organizations, manufacturing and distribution systems and research and development efforts.

Before I turn to the highlights of the past year, let me review our successful financial results in 2002. Cash flow from operations of $504 million was the result of strong earnings and focus on our balance sheet. We ended the year with net sales of $3,012 million, a 16 percent increase over 2001, and net earnings were $346 million, 29 percent above the prior year. Earnings before nonrecurring items rose 26 percent, to $357 million.

Strong Leadership Across Stryker's Groups

Recognizing that no company can continually innovate and execute without strong, broad-based leadership, in 2001 Stryker refined its organizational structure by completing the integration of all product and sales divisions into strategic, focused groups. In this process, we created two new groups, Stryker International and Stryker Biotech, Spine and Trauma. Our progress in 2002 has clearly validated this updated structure and highlighted the abilities of our four Group Presidents—Si Johnson of Stryker MedSurg, Jamie Kemler of Stryker Biotech, Spine and Trauma, Ron Lawson of Stryker International and Ned Lipes of Stryker Howmedica Osteonics. I would like to commend all of these talented individuals for their leadership and offer special thanks to Si Johnson for so ably taking on the role of Acting Chief Executive during my recovery from elective cardiac surgery early in the year.

Stryker's management capabilities are equally evident at the division level. In 2002, Stryker International's exemplary performance in critical markets around the world was driven principally by Luciano Cattani, President of Stryker Europe; Yoshi Nakazawa, President of Stryker Japan; and Andrew Fox-Smith, Vice President and General Manager of Stryker Pacific. Tim Scannell, Vice President and General Manager of Stryker Biotech, developed a highly skilled sales team for the Company's first biologic product. Stryker Spine President Mike Mainelli capably handled an acquisition that has strengthened Stryker's position in the high-growth spine market. Stryker Trauma President Vivian Masson led the introduction of a new intramedullary nail that has taken the market by storm. Bill Enquist, President of Stryker Endoscopy, achieved excellent sales results while relocating the division to a new, world-class facility. Jim Cunniff, Vice President and General Manager of Stryker Medical, introduced innovative products together with a unique delivery program that benefits hospitals. Jason Blackwood, President of Physiotherapy Associates, continued to make substantial gains in his division's competitive and complex marketplace.

By fine-tuning our organizational structure and tapping into the expertise, energy and leadership capabilities of these top managers, Stryker now has the best possible talent, leadership and focus to guide the Company through both the opportunities and challenges that lie before it.

A Confident Transition

At the corporate level, as well, Stryker has a deep leadership bench to draw on during times of transition. As of January 1, 2003, Dave Simpson, Stryker's long-time Chief Financial Officer, assumed the newly created post of Executive Vice President. In this role, Dave will focus his considerable talents on broad areas including investor relations, business development and strategic planning. Everyone connected with Stryker owes a debt of gratitude to Dave, whose strong financial management and business guidance have been invaluable since he joined the Company in 1987. During Dave's tenure as CFO, the Company's sales have increased 20-fold and net earnings have multiplied by a factor of 25. In addition, Dave has led the development of our financial organization to a level that has earned the respect of both the investment community and our industry peers. I would like to extend my personal thanks to Dave for his accomplishments and his continuing involvement with Stryker.

While Dave Simpson is the proverbial "tough act to follow," it was with pleasure and assurance that we promoted Dean Bergy to the post of Chief Financial Officer. Dean joined Stryker in 1994 as Controller and served as Vice President, Finance, for the Medical Division from 1996 to 1998, when he was promoted to Vice President, Finance, for the Company. In this key role, he led Stryker's internal financial management and reporting effort, all reporting to the Securities and Exchange Commission and the New York Stock Exchange and income tax planning and compliance. Dean also played a leading role in the 1998 acquisition of Howmedica, taking responsibility for all accounting and reporting during the transaction. Before joining Stryker, Dean was a Senior Manager with Ernst & Young LLP. He graduated from the University of Michigan and the Program for Management Development at Harvard Business School. I am very pleased to have Dean, with his talent, drive and character, as our new CFO.

High Standards in Financial Management

During 2002, much public attention was focused on financial reporting of publicly held companies, culminating in the passage of the Sarbanes-Oxley Act, which President Bush signed into law in July. As a company based in the fundamental values of honesty and integrity, Stryker holds to high standards of fiscal accountability, and we have always treated financial reporting as an integral part of managing our business. While we are taking steps to officially implement particular provisions, including formalizing our internal auditing function, our method of operation has consistently been in accord with the spirit and objectives of the new legislation and the related rule changes. With our accustomed level of scrutiny, we have intensely managed our balance sheet, as the annual improvement in our cash flow clearly demonstrates.

Key Developments

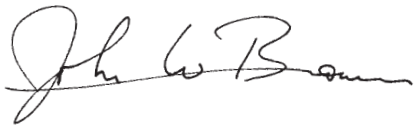
In July 2002, Stryker acquired the spinal implant business of Surgical Dynamics Inc. from Tyco International Ltd. This was a highly strategic acquisition for us, rounding out our spinal portfolio in the United States, where the market demand is greatest, and making us a more effective competitor in spine worldwide. We completely retired the debt from this $135 million transaction within three months, and we have now successfully completed the integration of Surgical Dynamics.

In another development, Stryker reached the decision to close its manufacturing facility in Rutherford, New Jersey, to eliminate excess capacity resulting from the acquisition of Howmedica. At the end of 2002, we were three months into a year-long phase-out of production at Rutherford. The transition is proceeding in an orderly fashion thanks to thorough negotiations with the union and a fair settlement. I appreciate the cooperation of the Rutherford employees in making this transition run so smoothly.

In February 2003, the U.S. Food and Drug Administration granted premarket approval for our Trident Ceramic Acetabular Insert in the United States. We are very pleased to bring this innovative product, which has enjoyed great clinical success in Europe, Canada and Australia, to U.S. surgeons and patients. We plan to launch the Trident insert in the second quarter of 2003.

This is a significant moment for Stryker. Our strategy of topflight products has been validated, and market trends are highly promising. Our senior management team is stronger than ever before. We are clearly focused on innovation, and we are recognizing those who are generating and executing new product ideas. These innovations will make a positive difference in patient outcomes, and they will help ensure that the outlook for Stryker continues to be favorable. As we look to the future, I would like to thank our employees for their dedication and our shareholders for their support.

Sincerely,



John W. Brown
Chairman, President and Chief Executive Officer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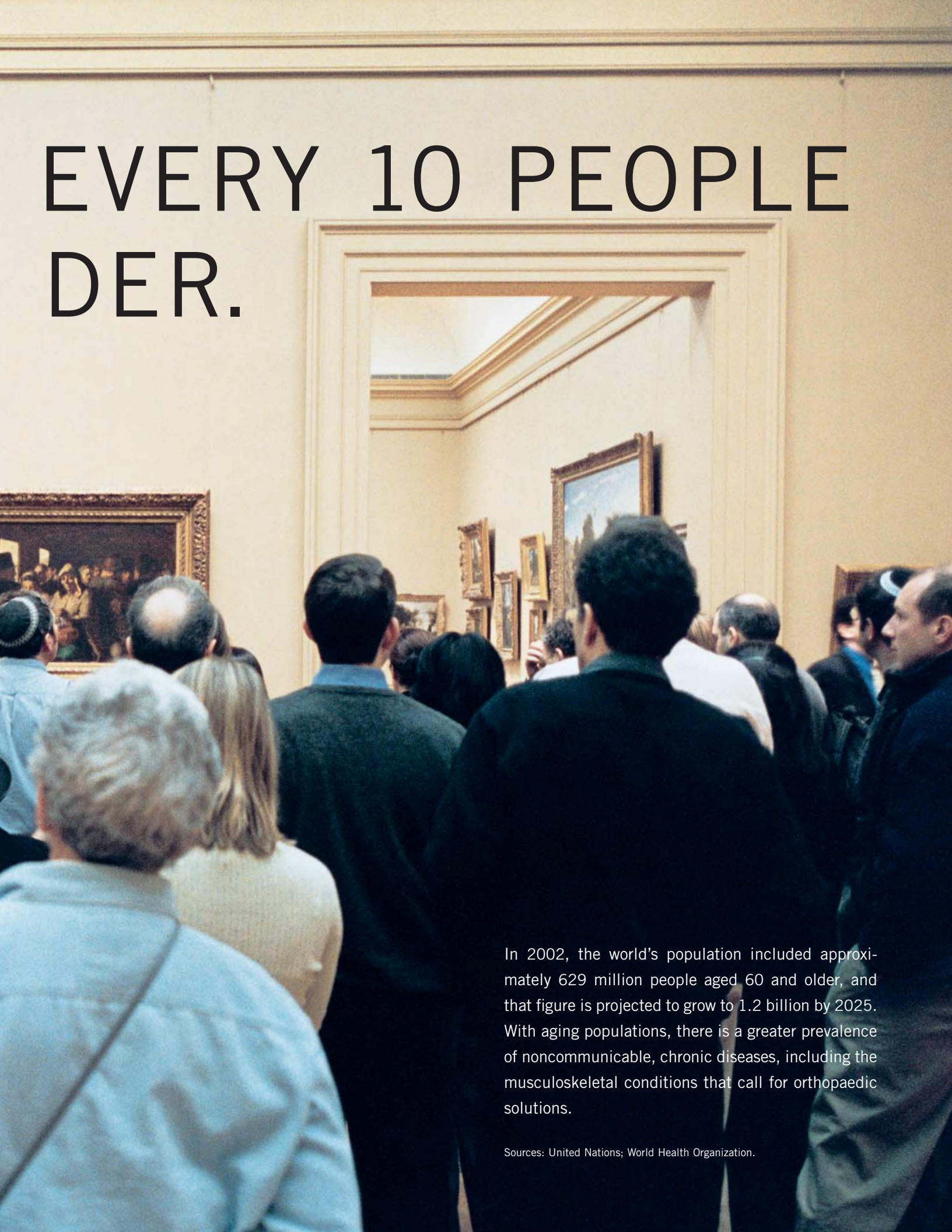


EVERY 10 PEOPLE DER.

In 2002, the world's population included approximately 629 million people aged 60 and older, and that figure is projected to grow to 1.2 billion by 2025. With aging populations, there is a greater prevalence of noncommunicable, chronic diseases, including the musculoskeletal conditions that call for orthopaedic solutions.

Sources: United Nations; World Health Organization.

Opportunity to Make a Difference

Stryker Corporation is dedicated to providing the global marketplace with best-in-class orthopaedic and medical products. Our portfolio of existing products, new product development initiatives, manufacturing and distribution infrastructure and strong relationships with thought leaders ideally position the Company to serve the world's rapidly aging population. Because the over-60 population has the greatest need for Stryker products, we now have an unprecedented opportunity to improve patient care and outcomes while increasing efficiency for surgeons and hospitals.

Aging Populations Drive Orthopaedic Demand

Around the world, aging is a defining factor of our time. As life expectancy increases, so does the prevalence of noncommunicable, chronic diseases that can be treated and managed over time. Musculoskeletal conditions—such as osteoarthritis, back pain and osteoporosis—magnify the need for Stryker's products for joint replacement, spinal surgery and fracture repair.

A comprehensive spinal portfolio

To better serve existing customers and attract new ones, Stryker seeks to provide comprehensive product portfolios. In 2002, the Company made important progress in broadening its spinal offerings with the acquisition of the spinal implant business of Surgical Dynamics Inc. (SDI), a division of Tyco International Ltd. The lead product acquired is the Ray Threaded Fusion Cage (TFC), which fills out our spinal portfolio by making us a full-line provider of spinal implant devices in the United States as well as internationally.

The Ray TFC device, used by surgeons for either posterior or anterior lumbar interbody fusion, has a strong track record—six years of clinical success with 150,000 implanted worldwide. By the end of 2002, thanks to dedicated teamwork, the successful integration of SDI and Stryker was complete, paving the way for us to compete more effectively in the rapidly growing global spine market.

Stryker also advanced its spinal business by introducing improved versions of leading products. The Xia Spinal System, our highly regarded system for thoracolumbar fusion, was upgraded with a lower profile screw and more ergonomic instrumentation, meeting with excellent customer response. Based on surgeon feedback, we also improved the screws and instrumentation of our popular Reflex Anterior Cervical Plate, used to stabilize the cervical spine for fusion.

We continued to extend our spinal organization in 2002, including the expansion of our implant manufacturing facility in France and the addition of an instrument production plant there. Also in France, we moved into an advanced Global Product Center that supports our expanded capabilities in engineering, marketing, regulatory affairs, quality assurance and training.

ScorpioFlex Single Axis Knee

Stryker Howmedica Osteonics

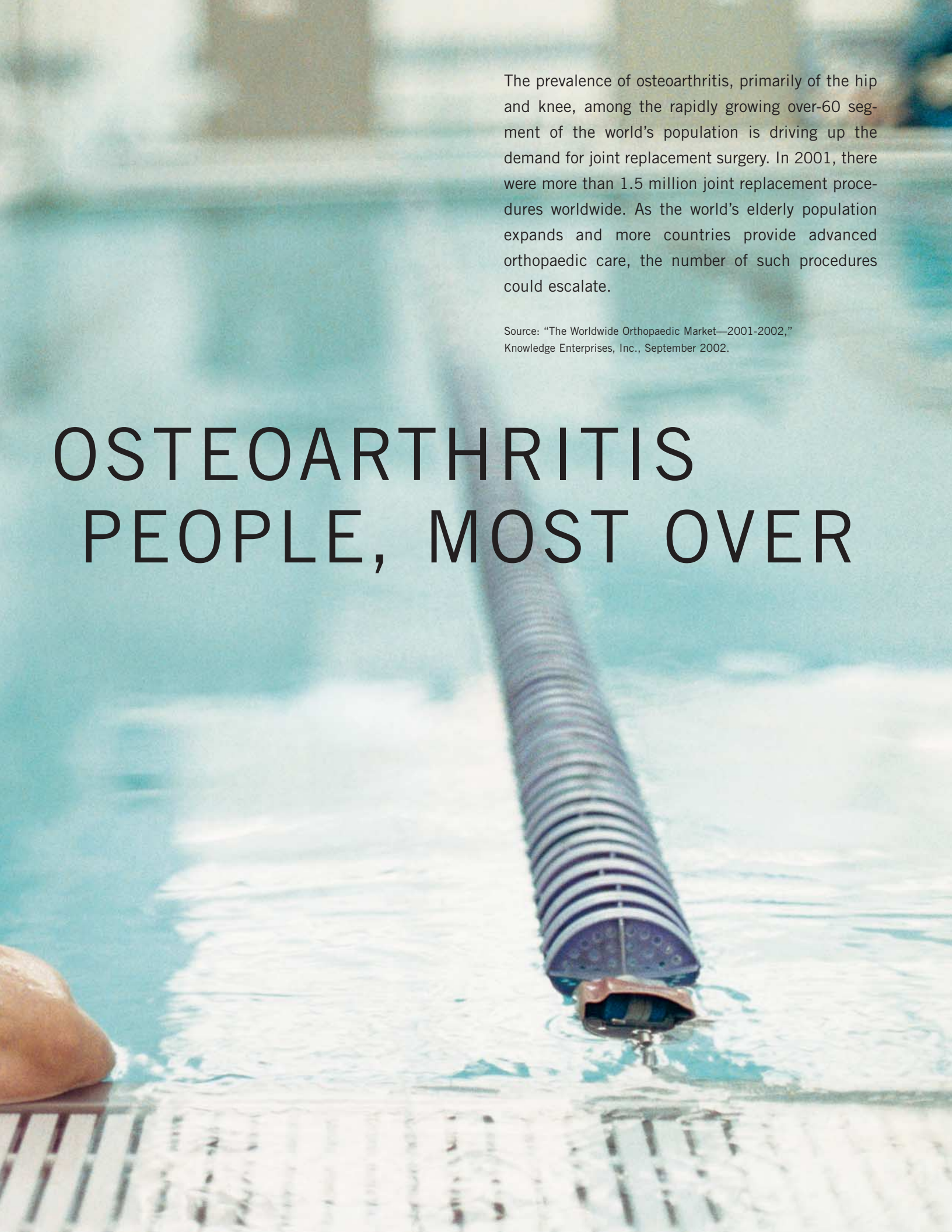
Stryker's Scorpio knee geometry has a patented single axis of rotation, a design feature that allows for easier leg extension and greater knee stability. In 2002, we expanded the Scorpio knee line with the ScorpioFlex knee system, which offers a maximized range of motion for motivated, more active patients. ScorpioFlex was originally designed for the Japanese market, where the culture requires a greater range of motion and flexion. This product's success in Japan led to its introduction in the United States.

EIUS Uni Knee System

Stryker Howmedica Osteonics

Stryker entered the minimally invasive knee market to great success with the EIUS implant, which experienced exponential sales growth in 2002 following its introduction in late 2001. This single-compartment implant is ideally suited for patients who are not yet candidates for the total knee replacement. It is designed to conserve bone where only one portion of the knee is worn. The system features precision instrumentation that allows for accurate alignment in a minimally invasive procedure. This approach can benefit patients by decreasing soft-tissue damage and hastening rehabilitation while offering hospitals a procedure that can shorten the length of stay.


AROUND THE GLOBE,
AFFECTS 190 MILLION
AGE 60.



The prevalence of osteoarthritis, primarily of the hip and knee, among the rapidly growing over-60 segment of the world's population is driving up the demand for joint replacement surgery. In 2001, there were more than 1.5 million joint replacement procedures worldwide. As the world's elderly population expands and more countries provide advanced orthopaedic care, the number of such procedures could escalate.

Source: "The Worldwide Orthopaedic Market—2001-2002," Knowledge Enterprises, Inc., September 2002.

OSTEOARTHRITIS PEOPLE, MOST OVER

Trident Acetabular System with Secur-Fit Hip Stem

Stryker Howmedica Osteonics

The Trident Acetabular System, with its patented locking mechanisms, has alternative Crossfire polyethylene and ceramic insert options to give surgeons intraoperative choices based on the needs of individual patients. In February 2003, we received premarket approval from the U.S. Food and Drug Administration for the Trident ceramic insert, which has been delivering excellent clinical results in Europe, Canada and Australia. U.S. patients can now receive hip implants with ceramic-on-ceramic surfaces, which in laboratory tests have demonstrated significantly lower wear than conventional surfaces and are therefore well suited to more active patients. The Trident Acetabular System is shown here with the Secur-Fit stem, which features our proprietary hydroxylapatite coating, Purefix HA. Also suited to the needs of active patients, Purefix HA has demonstrated more than 13 years of excellent clinical results in improving implant performance.

Biologics innovation with OP-1

Two decades ago, Stryker saw the potential that biologic products held for orthopaedics in an aging world and began a long-term investment in OP-1, a proprietary, recombinant version of the bone growth factor osteogenic protein-1. In 2001, OP-1 gained marketing authorization in the European Union and Australia and approval as a humanitarian device in the United States. The approved indications were specific to each jurisdiction, all involving difficult-to-heal long-bone fractures. Early in 2002, Canada approved OP-1 for nonunion fractures of long bones. Late in the year, following the creation of a relevant billing code by the Centers for Medicare & Medicaid Services, a major insurer issued a favorable policy coverage decision on reimbursement for the use of OP-1.

With these global approvals—the first of their kind—we began to market OP-1. In 2002, the jump in the number of patients treated demonstrated the success of our sales effort and the trust surgeons have developed in the product based on excellent patient outcomes. During 2002, more than 2,000 patients worldwide received implants of OP-1, more than the combined total from 1992 through 2001. In the United States, there was significant increase in demand in each quarter of 2002, and OP-1 is now used at more than 250 institutions, with multiple users at many of these sites. A one-time royalty fee paid in the fourth quarter eliminated the need for any further royalty payments, enhancing the prospects for the future profitability of the product.

Stryker is committed to the further development of OP-1 for spinal indications including spinal stenosis. This degenerative condition, which is widespread in the over-65 population, causes severe pain in the lower back and legs as a result of abnormal movement in the lower spine. Spinal fusion is used to stabilize the spine and reduce stenosis pain. Fusing the spine with OP-1 can eliminate the need for a preliminary surgery to take bone from the patient's hip to use in the fusion process.

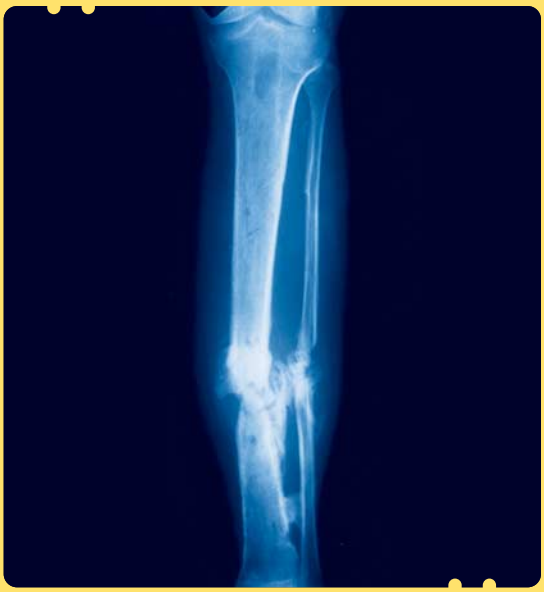
Currently, we are conducting a multicenter pivotal trial in the United States and Canada for posterolateral spine fusion using OP-1 to treat spinal stenosis. In 2002, we made significant progress in enrollment, which is expected to be completed in 2003. In Japan, we won approval to conduct a multicenter Phase 2 trial for the same indication and began enrolling patients. In the Japanese trial, OP-1 is being used in conjunction with screw and rod systems to fuse the spine.

OP-1

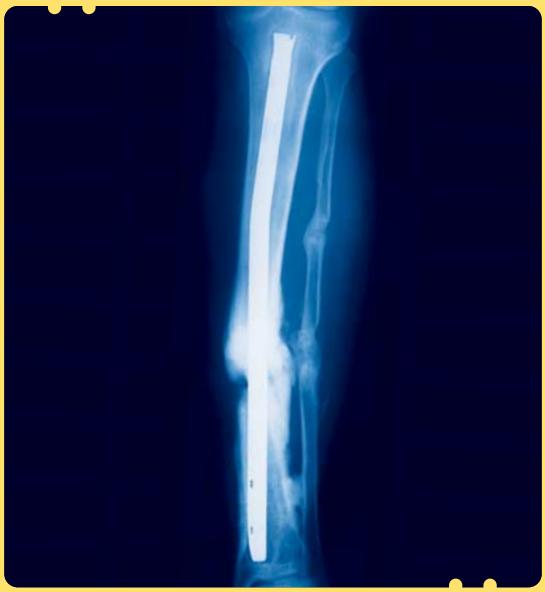
Stryker Biotech

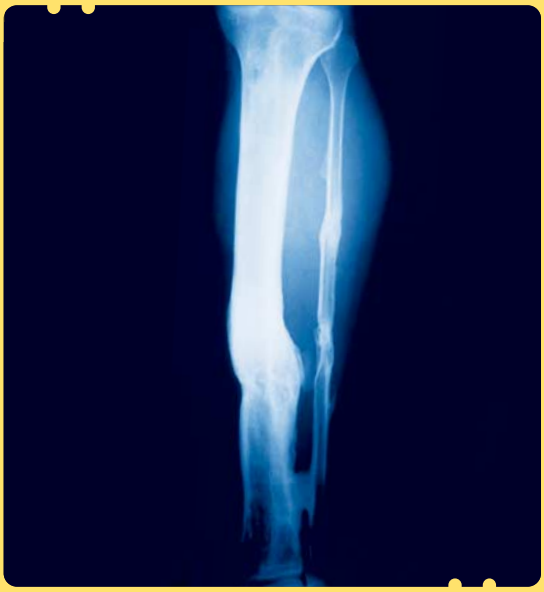
A decade ago, the first patient was treated with the OP-1 implant. X-ray images of this patient's tibia show remarkable bone regeneration since treatment, in contrast to a preoperative state for which the conventional treatment would have been amputation. With marketing authorization for OP-1 in the European Union, Australia and Canada and approval as a humanitarian device in the United States, all for indications involving difficult-to-heal long-bone fractures, we began an education-focused sales and marketing program. As a result, more than 2,000 patients worldwide were treated with OP-1 in 2002.

PRE-OP

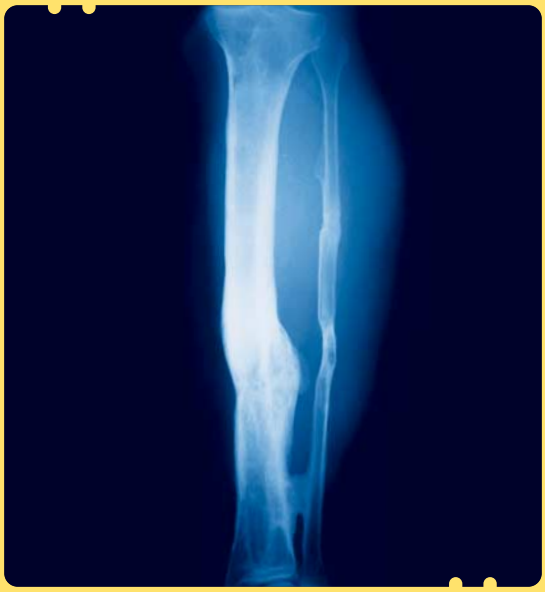


6 MONTHS





5 YEARS



10 YEARS

Accolade TMZF and C Hip Systems

Stryker Howmedica Osteonics

In 2002, Stryker introduced the Accolade C Cemented Hip System (at left in top photo) to complement the Accolade TMZF Cementless Hip System, which was launched the year before. These two femoral components share common basic instrumentation, so that the surgeon and operating room staff benefit from a high level of precision and outstanding efficiency. While the materials of the two femoral components differ, both hip implants feature increased material strength to allow for reduced neck geometry and therefore greater range of motion for patients. Together, the two Accolade hips offer surgeons more choice as they determine the best system for each individual candidate for total hip replacement.

EVERY 7 SECONDS, A BABY BOOMER TURNS 50.

The baby boom generation, born between 1947 and 1961, is advancing through middle age. This demographic juggernaut is characterized by its high level of education and demanding nature. These factors mean that patients of this generation are more knowledgeable about options, and that they expect better outcomes more quickly in order to resume normal functioning and active, pain-free lives.

Source: *Orthopedics Today,* November 2002.

Advances in fracture repair

In age-related fracture repair, Stryker's widely recognized leadership in intramedullary nailing technology is a key asset because of the prevalence of hip fractures among older individuals with osteoporosis. Stryker's Gamma Locking Nail, a family of products for hip fracture fixation with a stellar 14-year clinical history, serves this burgeoning market. Stryker has now leveraged this expertise and innovation with the new T2 IM Nailing System for the repair of long-bone fractures, which was launched in the United States, Europe and Japan in the second half of 2001.

Global view, regional strategies

Stryker approaches product development and manufacturing with a dual global and regional focus. In conjunction with dedicated regional sales and marketing organizations, this approach enables us to serve global needs while anticipating change within specific regions.

Our strong presence in Europe, for example, results from providing focused, country-by-country sales organizations supported by product lines suited to local preferences. The Exeter Total Hip System, with an outstanding 30-year clinical history, continues impressive growth and innovation. The introduction of a modified neck design for the Exeter system has increased range of motion and provides for a ceramic-on-ceramic bearing option.

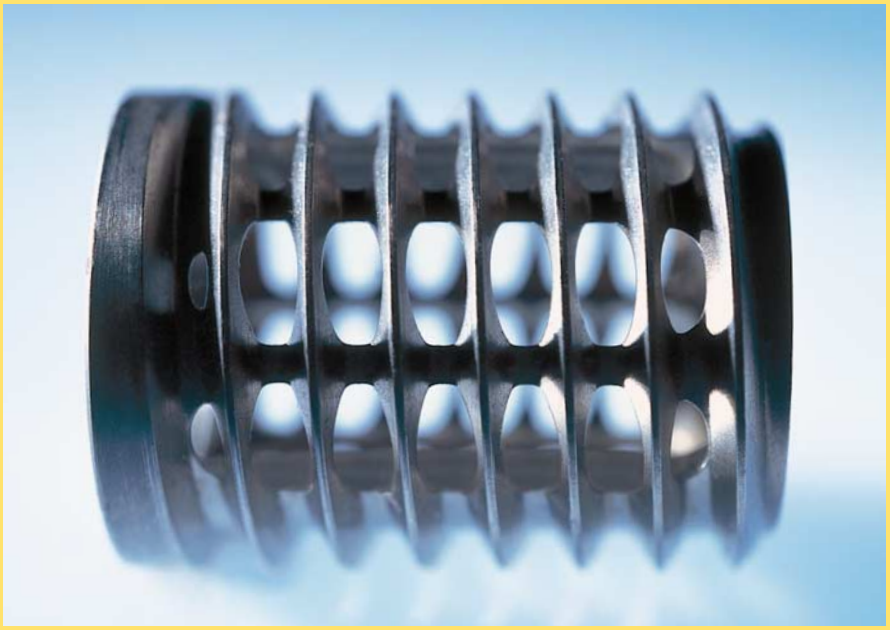
Stryker's approach accounted for a very good 2002 in Japan in spite of downward pricing pressures in that health-care system. This success was due to a range of implant products designed for the Japanese anatomy and lifestyle, supported by an increasingly specialized sales force and strong ties with surgical thought leaders. The Scorpio SuperFlex knee implant, launched in late 2001, was a star performer in 2002 because it offers the deep flexion typical in Japanese life. Similarly, the Super Secur-Fit Plus and Super EON hip systems provide the broad range of motion necessary for deep bending and stretching, and the T2 nail has been adjusted in both size and curvature to work with the Japanese anatomy.

The rollout of many of these products to the rest of Asia was a major force behind the exemplary performance of Stryker Pacific in 2002. Other factors included new leadership, heightened sales focus, additional emphasis on process and controls and a high degree of interaction with customers through sales and training.

Reflex Anterior Cervical Plate

Stryker Spine

The innovative Reflex system met with excellent customer acceptance in the United States and Europe at its launch in 2001. In 2002, we integrated suggestions from surgeons to improve the screws and instrumentation. The Reflex system, our entry into the cervical market, is used to stabilize the upper section of the spine to support fusion.



Ray Threaded Fusion Cage

Stryker Spine

In 2002, Stryker expanded its portfolio of spinal products with the acquisition of the Ray Threaded Fusion Cage (TFC), as well as other spinal products, from Surgical Dynamics Inc. This device is used for fusion of the lumbar spine in the treatment of degenerative disc disease and has been used in more than 150,000 procedures worldwide. The cage's unique internal architecture provides structural support intended to maintain disc height while promoting bone fusion and integration.

Xia Spinal System

Stryker Spine

The Xia Spinal System, used to fuse the thoracolumbar spine for stability and pain relief, has been highly popular since its introduction in 1999. In 2002, we advanced this product by reducing the profile of the screw and making ergonomic adjustments to the instrumentation. The improvements apply both to the titanium Xia system and the stainless steel version, which is used to address deformities including scoliosis.

Endosuite

Stryker Endoscopy

Stryker's pioneering work in bringing advanced, fully integrated technology to the operating room has resulted in hundreds of installed Endosuites. The suite shown here is located at The Orthopaedic Institute in San Antonio, Texas, which opened in April 2002. It features the latest generation of our communications technology, including telesurgery capabilities, which provide real-time remote access to conference rooms, classrooms, and operating rooms. Steve Burkhart, M.D., the Institute's founder, is one of the world's leading shoulder surgeons and regularly uses telesurgery as a tool for teaching surgeons around the world.


stryker


THROUGH BASIC
PROCESS IMPROVEMENTS,
A HOSPITAL
CAN SERVE UP TO 20%
MORE PATIENTS.

Efficiency is the watchword for hospitals today as they seek to serve more patients, often without the option of expansion. Hospitals can improve efficiency by implementing basic end-to-end process control measures that have long been used in other industries to deploy assets more effectively. Through such improvements, in less than one year a hospital can increase the number of patients it serves by up to 20%.

Source: *The McKinsey Quarterly,* 2001 Number 2.

System 5 Dual-Trigger Handpiece and Sagittal Saw

Stryker Instruments

Stryker continually fine-tunes and updates its surgical instruments to give clinicians optimal power, speed and choice. In 2002, Stryker released the fifth generation of its heavy-duty, battery-powered surgical instruments. The System 5 dual-trigger handpiece has separate triggers for forward and reverse, with an oscillation option. The System 5 sagittal saw is the only dual-speed saw on the market, providing the surgeon with a wider range of cutting alternatives.

Innovative solutions for active, demanding patients

Today's orthopaedic patients have higher expectations than ever before. As the leading edge of the baby boom generation passes age 50, its members demand prompt return to function so they can remain active and free of pain. In addition, osteoarthritis affects even younger people whose lifestyles have stressed their joints. These patients are more demanding, and they are better informed. We are ready for them, with advanced hip and knee implants featuring new materials and innovative designs.

Stryker pioneered high-performance, cementless hip systems incorporating such proprietary materials as Purefix HA coating, which has just completed 13 years of clinical use; Crossfire highly crosslinked polyethylene; the TMZF alloy; and ceramic-on-ceramic bearing surfaces. We also believe in supplying surgeons with options that span different patient needs and surgical situations. In 2002, for example, we introduced the Accolade C hip stem implant, a cemented partner of the cementless Accolade TMZF, which continues to be highly successful following its 2001 launch.

In a clear indication of the demand for return to function, in 2002 Stryker brought the SuperFlex knee, originally developed for the deep flexion needs of the Japanese market, to the United States, where it is known as ScorpioFlex. This implant is designed for active patients who have the ability and motivation to achieve postsurgical deep flexion.

Minimally invasive surgery, which hastens recovery because of less disruption to soft tissue, is another high-demand technology, as evidenced by the performance of the EIUS Uni Knee System. Designed for early intervention when only one portion of the knee is worn, this system facilitates a limited incision procedure. Launched in late 2001, the EIUS system had strong growth in 2002.

We are also developing the technology and instrumentation to support surgeon skills and new techniques in minimally invasive surgery for total knee replacement. In 2002, we designed instrumentation for our Scorpio knee system to support the technique pioneered by Peter Bonutti, M.D. We are now conducting a multicenter clinical study in order to validate the technique, which reportedly has resulted in faster rehabilitation, reduced pain and better function among Dr. Bonutti's patients.

Another innovative technology for improved patient outcomes is Stryker's Knee Navigation System, which offers more precise alignment and improved soft-tissue balancing in total knee replacement. We introduced this system in the United States in January 2002 following a successful European launch in mid-2001 and are now developing a next generation that is intended to increase both ease and speed of use.

The new generation of patients puts a high premium on freedom from pain. Two new Stryker products target pain management. The PainPump2 helps doctors and patients manage postsurgical pain across specialties. During recovery, the patient is trained to use the pump, including controlling

the amount of medication within parameters programmed by the clinician. We are also serving the interventional pain market with the DEKOMPRESSOR, used to treat back pain early and less invasively. Depending on the patient, this treatment may delay or eliminate the need for open surgery.

Physiotherapy Associates, our U.S. service division, helps patients achieve return to function through expertise in orthopaedics for all age groups. This division also has dedicated pediatric centers that use a multidisciplinary approach to serve children with developmental delays. Physiotherapy Associates had a year of steady growth, ending with 331 centers, an increase of 29 over 2001.

Helping Hospitals and Surgeons Deliver Their Best

Stryker's technology and innovation benefit hospitals and surgeons in their continuing drive for efficiency and safety as they seek to treat more patients. In orthopaedic specialties, simpler, more standardized implant instrumentation is key to greater efficiency. Stryker has invested in improving instrumentation across its hip, knee, spinal and trauma implants. In 2002, we completed the Accolade hip system and launched the Universal Mandible System, both with innovative, streamlined instrumentation.

We also continuously improve our products to give surgeons greater choice and control. The System 5, the fifth generation of our leading heavy-duty, battery-powered instruments for total joint replacement, was introduced to immediate acclaim in 2002. Our surgical navigation systems also provide surgeons with greater control through unique two-way communication between the surgical instrument and the camera. We now offer navigation systems for functional neurosurgery, total knee replacement and applications in spinal, trauma and ear, nose and throat specialties.

Stryker has pioneered the operating room of the future, offering surgeons and hospitals greater efficiency through leading-edge imaging and communications. In the decade since we first introduced the Endosuite, a fully functional operating room that supports less invasive surgery across all specialties, we have continued to innovate by adding and improving technology. In 2002, we introduced the SDC Pro 2 DVD, which allows the surgeon to record an entire case to a broadcast-quality DVD while capturing and printing still images for the patient's chart and saving images and video directly to the hospital network. With our established leadership in operating room technology, we are primed to apply the integrated Endosuite concept to an even greater range of specialties.

Stryker's patient handling equipment promotes both efficiency and patient and staff safety. We recently introduced the Zoom stretcher, which helps staff members handle heavier patients while minimizing the risk of back injury. Additionally, the Chaperone bed exit system not only helps keep patients safe, but by substantially reducing false alarms, it saves steps for nurses.

Zoom Stretcher

Stryker Medical

Many hospitals face patient handling challenges, particularly with today's widespread nursing shortages. Patients tend to be heavier, and many facilities have ramps and long hallways. These factors increase the risk of back injury for nurses and other hospital staff. Stryker addressed these challenges with the introduction of the Zoom stretcher. This product combines our self-propelling drive system from our Zoom bed technology with our Big Wheel stretcher technology, which reduces maximum startup force by 50 percent and turning effort by 60 percent. These features help reduce the risk of back strain. One person can handle the stretcher—a great asset in periods of low staffing.

T2 IM Nailing System

Stryker Trauma

The T2 IM Nailing System for long-bone fracture repair produced outstanding sales results in 2002, its first full year on the market in the United States, Europe and Japan. Beyond the design and manufacturing quality of the nails themselves, the system is notable for a common instrument platform for the femur, tibia and humerus that combines ease of use with a high degree of accuracy.

Universal Mandible Plating System

Stryker Leibinger

Stryker's new comprehensive system for jaw reconstruction and fracture repair has been well received for both its technological advances and ease of use. The system features our unique SMARTLock screw technology that provides a secure lock while allowing more flexibility in the angle of placement. In contrast to other systems, a single screwdriver blade works with all screws. Ease of use is further enhanced by color coding of plates, screws and instruments.

FINANCIAL REVIEW

(dollars in millions, except per share amounts)

SUMMARY OF OPERATIONS	*2002*	*2001*	*2000*
Net sales	$3,011.6	$2,602.3	$2,289.4
Cost of sales:			
Before inventory step-up	1,111.2	963.8	815.2
Inventory step-up	–	–	–
Total cost of sales	1,111.2	963.8	815.2
Gross profit	1,900.4	1,638.5	1,474.2
Research, development and engineering expenses	141.4	142.1	122.2
Selling, general and administrative expenses	1,165.4	985.4	885.6
Purchased research and development	–	–	–
Restructuring, acquisition-related and special charges (credits)	17.2	0.6	(1.0)
Gain on patent judgment	–	–	–
	1,324.0	1,128.1	1,006.8
Other expense (income)	69.7	104.7	132.5
Earnings before income taxes and extraordinary item	506.7	405.7	334.9
Income taxes	161.1	133.9	113.9
Earnings before extraordinary item	345.6	271.8	221.0
Extraordinary loss, net of income taxes	–	(4.8)	–
Net earnings	$345.6	$267.0	$221.0
Net earnings per share of common stock[a]:			
Basic	$1.75	$1.38[b]	$1.13
Diluted	$1.70	$1.34[b]	$1.10
Dividend per share of common stock[a]	$.12	$.10	$.08
Average number of shares outstanding – in millions[a]:			
Basic	197.5	196.3	195.1
Diluted	203.8	203.0	201.1

(a) Adjusted for the two-for-one stock splits effective June 10, 1996 and May 12, 2000.
(b) Excludes net extraordinary loss per share of $.02 basic and $.02 diluted.

FINANCIAL AND STATISTICAL DATA	*2002*	*2001*	*2000*
Cash and marketable securities	37.8	50.1	54.0
Working capital	443.8	459.7	379.6
Current ratio	1.6	1.9	1.6
Property, plant and equipment – net	519.2	444.0	378.1
Capital expenditures	139.0	161.9	80.7
Depreciation and amortization	186.1	172.0	168.6
Total assets	2,815.5	2,423.6	2,430.8
Long-term debt, including current maturities	501.7	722.6	1,012.5
Stockholders' equity	1,498.2	1,056.2	854.9
Return on average equity	27.1%	27.9%	29.0%
Net cash provided by operating activities	503.9	468.3	331.8
Number of stockholders of record	2,983	2,886	2,904
Number of employees	14,045	12,839	12,084

1999	*1998*	*1997*	*1996*	*1995*	*1994*	*1993*
$2,103.7	$1,103.2	$980.1	$910.1	$871.9	$681.9	$557.3
791.5	464.3	397.7	392.4	369.4	300.4	256.7
198.2	7.8	–	–	–	–	–
989.7	472.1	397.7	392.4	369.4	300.4	256.7
1,114.0	631.1	582.4	517.7	502.5	381.5	300.6
105.2	61.0	56.9	56.9	43.8	39.6	36.2
808.4	373.6	334.3	326.6	301.4	221.4	172.4
–	83.3	–	7.5	–	–	–
18.9	19.0	–	34.3	–	–	–
–	–	–	(61.1)	–	–	–
932.5	536.9	391.2	364.2	345.2	261.0	208.6
151.7	3.3	(4.1)	(12.6)	3.4	(2.7)	(4.1)
29.8	90.9	195.3	166.1	153.9	123.2	96.1
10.4	30.9	70.0	61.6	66.9	50.8	35.9
19.4	60.0	125.3	104.5	87.0	72.4	60.2
–	–	–	–	–	–	–
$19.4	$60.0	$125.3	$104.5	$87.0	$72.4	$60.2
$.10	$.31	$.65	$.54	$.45	$.37	$.31
$.10	$.31	$.64	$.53	$.44	$.37	$.31
$.065	$.06	$.055	$.05	$.023	$.02	$.018
193.8	192.6	192.5	193.7	193.9	193.5	193.4
198.6	196.3	196.3	196.9	197.1	196.1	195.7

1999	*1998*	*1997*	*1996*	*1995*	*1994*	*1993*
83.5	138.6	351.1	367.6	264.6	202.0	152.6
440.8	666.2	433.7	501.8	448.8	361.3	214.0
1.7	2.0	2.4	3.0	3.6	3.0	2.6
391.5	429.5	163.9	172.3	182.6	180.7	67.7
76.4	51.3	35.2	26.7	36.3	29.2	20.2
162.8	53.2	49.5	34.7	28.7	20.9	16.2
2,580.5	2,875.4	985.1	993.5	854.9	768.0	454.2
1,287.4	1,503.0	78.1	93.9	100.0	100.6	32.2
671.5	672.6	612.8	530.4	454.3	358.3	288.4
2.9%	9.3%	21.9%	21.2%	21.4%	22.4%	23.1%
284.0	154.5	91.9	204.3	111.5	97.7	86.1
2,929	3,061	3,127	3,306	3,260	3,684	3,951
10,925	10,974	5,691	5,274	4,629	4,221	3,228

Results of Operations

The table below outlines the components of the consolidated statements of earnings as a percentage of net sales and the year-to-year percentage change in dollar amounts:

	Percentage of Net Sales			Percentage Change	
	2002	*2001*	*2000*	*2002/01*	*2001/00*
Net sales	100.0%	100.0%	100.0%	16%	14%
Cost of sales	36.9	37.0	35.6	15	18
Gross profit	63.1	63.0	64.4	16	11
Research, development and engineering expenses	4.7	5.5	5.3	–	16
Selling, general and administrative expenses	38.7	37.9	38.7	18	11
Restructuring and acquisition-related charges	0.6	–	–	–	–
Other expense (income)	2.3	4.0	5.8	(33)	(21)
Earnings before income taxes and extraordinary item	16.8	15.6	14.6	25	21
Income taxes	5.3	5.1	5.0	20	18
Earnings before extraordinary item	11.5	10.4	9.7	27	23
Extraordinary loss, net of income taxes	–	(0.2)	–	–	–
Net earnings	11.5%	10.3%	9.7%	29	21

The table below sets forth domestic/international and product line sales information:

	Net Sales (*in millions*)			Percentage Change	
	2002	*2001*	*2000*	*2002/01*	*2001/00*
Domestic/international sales					
Domestic	$1,973.7	$1,688.4	$1,408.2	17%	20%
International	1,037.9	913.9	881.2	14	4
Total net sales	$3,011.6	$2,602.3	$2,289.4	16	14
Product line sales					
Orthopaedic Implants	$1,704.8	$1,447.2	$1,315.6	18	10
MedSurg Equipment	1,105.3	974.2	826.5	13	18
Physical Therapy Services	201.5	180.9	147.3	11	23
Total net sales	$3,011.6	$2,602.3	$2,289.4	16	14

2002 Compared with 2001

Stryker Corporation's net sales increased 16% in 2002 to $3,011.6 million from $2,602.3 million in 2001. Net sales grew by 11% as a result of increased unit volume and changes in product mix; 3% related to higher selling prices; and 2% as a result of acquired businesses.

Domestic sales were $1,973.7 million for 2002, representing an increase of 17% as a result of strong shipments of Orthopaedic Implants and MedSurg Equipment and higher revenue from Physical Therapy Services. The July 1, 2002, acquisition of the Surgical Dynamics Inc. spinal implant business (SDI) from Tyco International Ltd. added $22.8 million to domestic sales for 2002. International sales were $1,037.9 million for 2002, representing an increase of 14% as a result of

higher shipments of Orthopaedic Implants and MedSurg Equipment. The acquisition of SDI added $2.5 million to international sales for 2002. The impact of foreign currency comparisons to the dollar value of international sales was favorable by $13.7 million for 2002. Excluding the impact of foreign currency, international sales increased 12% in 2002.

Worldwide sales of Orthopaedic Implants were $1,704.8 million for 2002, representing an increase of 18% as a result of higher shipments of reconstructive (hip, knee and shoulder), trauma and spinal implants. Excluding the impact of foreign currency, sales of Orthopaedic Implants increased 17% in 2002. Worldwide sales of MedSurg Equipment were $1,105.3 million for 2002, representing an increase of 13% as a result of higher shipments of powered surgical instruments, endoscopic systems, hospital beds and stretchers and Leibinger craniomaxillofacial implants and image-guided surgical systems. Excluding the impact of foreign currency, sales of MedSurg Equipment increased 13% in 2002. Physical Therapy Services revenues were $201.5 million for 2002, representing an increase of 11% as a result of new physical therapy centers and higher revenue from existing centers.

Cost of sales represented 36.9% of sales compared with 37.0% in 2001. The slightly lower cost of sales percentage in 2002 is due to an increase in the absorption of fixed manufacturing costs caused by increased production at certain of the Company's manufacturing plants to meet current demand and higher sales growth for the higher margin Orthopaedic Implant products, offset partially by higher product obsolescence resulting from product launches.

While research, development and engineering expenses in 2002 were consistent with prior year amounts, they decreased to 4.7% of sales from 5.5% in 2001. Research, development and engineering spending was affected in 2002 by the commercial launch of the osteogenic protein-1 (OP-1) product, which occurred in various markets in the second and fourth quarters of 2001. Following the launch, in 2002 Stryker Biotech recorded a greater proportion of its expenses as cost of sales and selling, general and administrative expenses, compared with 2001 when this division classified substantially all of its costs as research, development and engineering. Increased spending from the Company's continued focus on new product development partially offset the decreased research, development and engineering expenses related to Stryker Biotech. New product introductions in 2002 included ScorpioFlex knee for the United States market, Super Secur-Fit Plus hip for the Japanese market, Trident Ceramic Acetabular Hip System in Canada, Xia II Spinal System, System 5 heavy-duty, battery-powered system, TPS Saber Drill, SDC Pro 2 surgical DVD documentation system, PainPump2, Precision System for percutaneous cement delivery, fluoroscopic software module for the Stryker Navigation System and Go Bed +.

Selling, general and administrative expenses increased 18% in 2002 and represented 38.7% of sales compared with 37.9% in 2001. The increase in selling, general and administrative expense is partially due to an increase in sales commission expense as a result of the 16% increase in net sales in 2002. In addition, the Company incurred an $8.9 million increase in insurance costs during 2002. The change in classification of certain Stryker Biotech expenses, as discussed above, also contributed to the increase in selling, general and administrative expenses. Discount expense related to the accounts receivable securitization program, which is included in selling, general and administrative expenses, declined to $2.7 million in 2002 from $5.8 million in 2001 as a result of lower discount rates.

The Company recognized charges of $17.2 million in continuing operations ($11.5 million net of income taxes) relating to restructuring and acquisition-related items in the third quarter of 2002 and restructuring and acquisition-related charges of $0.6 million in the fourth quarter of 2001. The 2002 restructuring and acquisition-related items include a charge of $21.0 million ($14.1 million net of income taxes) for employment-related costs to close the Company's Rutherford, New Jersey manufacturing facility, partially offset by a credit of $3.8 million ($2.6 million net of income taxes) to reverse certain Howmedica restructuring and acquisition-related costs to reflect actual final payments required. The $21.0 million restructuring charge relates to the shutdown agreement reached between the Company and the employee bargaining unit to close the Howmedica Osteonics implant manufacturing facility in Rutherford, New Jersey which was ratified by the members of the I.U.E.-CWA Local 485 on August 23, 2002. Under the agreement, laid-off employees will receive significantly more benefits than they would have under the Collective Bargaining Agreement that was set to expire on August 31, 2002. In addition, at least 80 qualified employees from the Rutherford facility will be offered employment at the new Howmedica Osteonics facility in Mahwah, New Jersey.

The charge covers employment-related severance costs for approximately 400 employees. The Company expects the Rutherford facility to be closed over the next 12 months with final severance payments to be made in 2004. As Howmedica Osteonics prepares to permanently cease manufacturing in Rutherford, it will transition production to its facilities in Mahwah, New Jersey as well as Cork and Limerick, Ireland.

In the fourth quarter of 2001, the Company recognized charges of $0.6 million in continuing operations related to various restructuring and acquisition-related events. The 2001 restructuring and acquisition-related charges included $2.4 million of charges, partially offset by the reversal of prior year restructuring accruals totaling $1.8 million. See the following comparison of 2001 results to 2000 results for additional information.

Interest expense declined to $40.3 million in 2002 from $67.9 million in 2001, primarily as a result of lower outstanding debt balances. The decrease in intangibles amortization to $28.9 million in 2002 from $38.4 million in 2001 is primarily the result of the Company's adoption of Financial Accounting Standards Board (FASB) Statement No. 142, *Goodwill and Other Intangible Assets,* which prohibits the amortization of goodwill. If the nonamortization provisions of Statement No. 142 had been applied in the prior year, amortization expense for 2001 would have been reduced by $18.1 million and net earnings would have increased by $12.1 million ($.06 per diluted share). Other expense was $0.5 million in 2002, compared with $1.6 million of other income in 2001 due to foreign currency transaction losses in the current year versus gains in the prior year, partially offset by higher interest income.

The effective income tax rate was 31.8% in 2002 compared with 33.0% in 2001. The Company's effective income tax rate for the year was reduced from 33.0% to 31.8% in the fourth quarter of 2002, thereby reducing income tax expense by $6.1 million, primarily as a result of increased manufacturing in lower tax jurisdictions such as Ireland and Puerto Rico.

Earnings before extraordinary item increased 27% to $345.6 million from $271.8 million in 2001; basic earnings per share before extraordinary item increased 27% to $1.75 in 2002 from $1.38 in 2001; and diluted earnings per share before extraordinary item increased 27% to $1.70 in 2002 from $1.34 in 2001. In December 2001, the Company refinanced and prepaid the remaining $642.7 million outstanding under the $1,650.0 million Senior Secured Credit Facilities established in 1998 in connection with the Howmedica acquisition. The prepayment of the 1998 Facilities resulted in the write-off in 2001 of related unamortized deferred loan costs of $7.1 million, which was reflected as an extraordinary loss of $4.8 million (net of income taxes of $2.3 million; $.02 per basic and diluted share). Net earnings were $345.6 million (basic and diluted net earnings per share of $1.75 and $1.70, respectively) compared with $267.0 million (basic and diluted net earnings per share of $1.36 and $1.32, respectively) in 2001.

Excluding nonrecurring items that include the impact of the restructuring and acquisition-related items on 2002 and 2001 and the impact of the change in goodwill amortization and the extraordinary loss on 2001, net earnings in 2002 were $357.1 million, representing a 26% increase over net earnings of $284.3 million in 2001. Diluted net earnings per share increased 25% to $1.75 compared with $1.40 in 2001. The reconciliations, including related earnings per share amounts, of reported net earnings to adjusted net earnings before nonrecurring items are as follows:

	Years ended December 31 *(in millions)*		
	2002	*2001*	*% Change*
Reported net earnings	$345.6	$267.0	29
Restructuring and acquisition-related items	11.5	0.4	–
Goodwill and assembled workforce amortization	–	12.1	–
Extraordinary loss	–	4.8	–
Adjusted net earnings before nonrecurring items	$357.1	$284.3	26
Basic net earnings per share:			
Reported basic net earnings per share	$1.75	$1.36	29
Restructuring and acquisition-related items	$.06	–	–
Goodwill and assembled workforce amortization	–	$.06	–
Extraordinary loss	–	$.02	–
Adjusted basic net earnings per share before nonrecurring items	$1.81	$1.45	25
Diluted net earnings per share:			
Reported diluted net earnings per share	$1.70	$1.32	29
Restructuring and acquisition-related items	$.06	–	–
Goodwill and assembled workforce amortization	–	$.06	–
Extraordinary loss	–	$.02	–
Adjusted diluted net earnings per share before nonrecurring items	$1.75	$1.40	25

2001 Compared with 2000

Stryker Corporation's net sales increased 14% in 2001 to $2,602.3 million from $2,289.4 million in 2000. Net sales grew by 12% as a result of increased unit volume and changes in product mix; 3% related to higher selling prices; 1% as a result of acquired businesses; and 1% related to the inclusion of freight revenue in net sales in 2001. Freight revenue was recorded as an offset to cost of sales during 2000. These increases were partially offset by a 3% decline due to changes in foreign currency exchange rates.

The Company's domestic sales increased 20% in 2001 to $1,688.4 million from $1,408.2 million in 2000. The domestic sales gain was the result of higher shipments of Orthopaedic Implants, MedSurg Equipment and higher revenue from Physical Therapy Services. International sales increased 4% for the year to $913.9 million from $881.2 million in 2000 as a result of higher shipments of Orthopaedic Implants and MedSurg Equipment. The impact of foreign currency comparisons on the dollar value of international sales was unfavorable by $62.1 million for the year. Excluding the impact of foreign currency, international sales increased 11% in 2001.

Worldwide sales of Orthopaedic Implants were $1,447.2 million for 2001, representing an increase of 10% as a result of higher shipments of reconstructive (hip, knee and shoulder), trauma and spinal implants. Excluding the impact of foreign currency, sales of Orthopaedic Implants increased 13% in 2001. Worldwide sales of MedSurg Equipment were $974.2 million for 2001, representing an increase of 18% based on higher shipments of powered surgical instruments, endoscopic systems, hospital beds and stretchers and Leibinger craniomaxillofacial implants and image-guided surgical systems. Excluding the

impact of foreign currency, sales of MedSurg Equipment increased 20% in 2001. Physical Therapy Services revenues were $180.9 million for 2001, representing an increase of 23% as a result of new physical therapy centers and higher revenue from existing centers.

Cost of sales represented 37.0% of sales compared with 35.6% in 2000. The higher cost of sales percentage in 2001 resulted primarily from the change in recording of freight revenue described above and the classification of certain shipping costs as cost of sales in 2001 that had been reported in selling, general and administrative expenses in the prior year. The cost of sales percentage increased approximately 1.0% in 2001 as a result of the change in classification of freight revenue and shipping costs. Cost of sales for 2001 was also higher by approximately 0.4% due to an increase in unabsorbed manufacturing costs caused by the slowing of production in certain of the Company's manufacturing plants to reduce overall inventory levels. The Company continually assesses the overall capacity provided by its manufacturing plants relative to cost, inventory management and expected sales growth. A slight increase in Orthopaedic Implant margins was more than offset by higher sales and revenues of lower-margin MedSurg Equipment products and Physical Therapy Services.

Research, development and engineering expenses increased 16% in 2001 and represented 5.5% of sales compared with 5.3% in 2000. The increase in research, development and engineering spending in 2001 resulted from continued Company-wide focus on new product development. New product introductions in 2001 included the Accolade Cemented Hip Stem, EIUS minimally invasive Uni Knee, T2 Intramedullary Nail System, Reflex Anterior Cervical Plate, Percutaneous Cement Delivery System, Elite Attachments for TPS, Cordless Driver II, Stryker Knee Navigation System, SDC Pro 2 surgical documentation system, 988 Digital Camera, Go Bed, Trio Mobile Surgery Platform and an enhanced Secure II bed. In the second quarter of 2001, the Company received marketing approval for its OP-1 product in Australia and the European Union. The approved indication in Australia was for the treatment of nonunion of long bone fractures secondary to trauma for the purposes of initiating repair by new bone formation. The approved indication in Europe was for tibial nonunions of nine-month duration, secondary to trauma, in skeletally mature patients, in cases where previous treatment with autograft has failed or use of autograft is unfeasible. In the fourth quarter of 2001, the Company was granted Humanitarian Device Exemption (HDE) status for OP-1 by the United States Food and Drug Administration (FDA). The approved indication in the United States was for use as an alternative to autograft in recalcitrant long bone nonunions where use of autograft is unfeasible and alternative treatments have failed. Under the HDE, OP-1 has been made available as a humanitarian device, defined by the FDA as one intended to benefit patients by treating or diagnosing a disease or condition that affects fewer than 4,000 individuals per year in the United States. The first commercial sales of OP-1 in Australia began in mid-May 2001 and the commercial launch of OP-1 in select markets of the European Union began in August. The first sales of OP-1 in the United States under the HDE began in November. The commercial launch of OP-1 did not have a significant impact on sales in 2001.

Selling, general and administrative expenses increased 11% in 2001 and represented 37.9% of sales compared with 38.7% in 2000. The classification of certain shipping costs as cost of sales in 2001 reduced selling, general and administrative expenses as a percent of sales by approximately 0.4% in 2001. In addition, discount expense related to the accounts receivable securitization program, which was included in selling, general and administrative expenses, declined to $5.8 million in 2001 from $7.1 million in 2000 as a result of lower discount rates.

The Company recognized charges of $0.6 million in continuing operations relating to various restructuring and acquisition-related events in the fourth quarter of 2001 and recognized restructuring and acquisition-related credits of $1.0 million in 2000. The 2001 restructuring and acquisition-related charges include $2.4 million of charges, partially offset by the reversal of prior year restructuring accruals totaling $1.8 million. The $2.4 million in 2001 charges included a $0.9 million acquisition-related charge for severance and related costs associated with the reorganization of the Company's sales structure in Italy to accommodate the integration of the business acquired from the Company's independent Italian distributor. The reorganization established a direct sales force in Italy that distributes the Company's full product portfolio. The $0.9 million charge covered severance costs for three employees in Italy and costs to cancel contracts with discontinued agents. The reorganization of the sales structure in Italy was completed in the first quarter of 2002. The 2001 charge also included a $0.7 million

charge related to the reorganization of the Company's distribution channels in Latin America and $0.8 million for severance costs for 10 employees in Europe. The $0.7 million charge reflected the cost to terminate a distributor and was based on contractual terms. Planned European workforce reductions were completed in the first quarter of 2002. The $1.8 million in credits included $1.4 million related to a reduction in the expected costs to complete headcount reductions associated with the 2000 and 1999 reorganizations of the Company's European and Japanese distribution operations. The 2001 credits also included $0.4 million to reverse the remaining loss reserves established in Japan for discontinued ophthalmology inventories sold on a contingent basis in 1999.

In 2000, the Company recognized credits of $1.0 million, consisting of the reversal of prior year restructuring accruals totaling $7.0 million, partially offset by charges totaling $6.0 million. The $7.0 million in credits included $1.2 million related to the reorganization of Stryker's distribution channels associated with the acquisition of Howmedica and $2.7 million to reverse reserves for a distributor reorganization that was charged to operations in 1996. The credits also included $2.7 million related to a reduction in the expected costs to complete headcount reductions in Japan and $0.4 million to reverse a portion of loss reserves established in Japan for discontinued ophthalmology inventories sold on a contingent basis in 1999. The $6.0 million in 2000 restructuring charges included a $4.0 million charge to cover severance costs for 95 employees, primarily in Europe; $1.4 million for asset write-offs, primarily for goodwill and inventory, and lease commitments associated with certain operations, principally in Europe, that were closed in the fourth quarter of 2000. The planned workforce reductions were completed in 2001, and the remaining amount of the reserve was reversed in 2001. The 2000 restructuring charges also included $0.6 million to terminate two small European distributors.

Interest expense declined to $67.9 million in 2001 from $96.6 million in 2000, primarily as a result of lower outstanding debt balances. The increase in intangibles amortization to $38.4 million in 2001 from $34.7 million in 2000 related primarily to business acquisitions during 2001 and the second half of 2000. Other income increased to $1.6 million in 2001 from other expense of $1.2 million in 2000, primarily as a result of foreign currency transaction gains in 2001 versus foreign currency transaction losses in 2000, partially offset by lower interest income. The effective income tax rate for 2001 was 33.0% compared with a 34.0% effective income tax rate in 2000. The decrease in the rate from 2000 to 2001 was attributable to the mix of operating results among the tax jurisdictions.

Earnings before extraordinary item increased 23% to $271.8 million in 2001 from $221.0 million in 2000; basic earnings per share before extraordinary item increased 22% to $1.38 in 2001 from $1.13 in 2000; and diluted earnings per share before extraordinary item increased 22% to $1.34 in 2001 from $1.10 in 2000. In December 2001, the Company refinanced and prepaid the remaining $642.7 million outstanding under the $1,650.0 million Senior Secured Credit Facilities established in 1998 in connection with the Howmedica acquisition. The prepayment of the 1998 Facilities resulted in the write-off of related unamortized deferred loan costs of $7.1 million, which was reflected as an extraordinary loss of $4.8 million (net of income taxes of $2.3 million; $.02 per basic and diluted share). Net earnings were $267.0 million (basic and diluted net earnings per share of $1.36 and $1.32, respectively) compared with $221.0 million (basic and diluted net earnings per share of $1.13 and $1.10, respectively) in 2000.

Liquidity and Capital Resources

The Company's working capital at December 31, 2002 decreased $15.9 million to $443.8 million from $459.7 million at December 31, 2001. The working capital decrease is due primarily to lower cash balances, additional liabilities resulting from restructuring and acquisition-related items recorded during 2002 and increases in other accrued liabilities, partially offset by increases in accounts receivable and inventories. The additional liabilities from restructuring and acquisition-related items is the result of the aforementioned pending closure of the Company's Rutherford, New Jersey manufacturing facility. Other accrued liabilities increased in 2002 as a result of higher obligations for third-party sales agent commissions, third-party royalties, non-income-based taxes and general increases in other accrued liabilities. Accounts receivable days sales outstanding, excluding the effect of the Company's $130.0 million accounts receivable securitization program, decreased 1 day to 58 days at December 31, 2002 from 59 days at December 31, 2001. The lower days sales outstanding at December 31, 2002 is the result of improved

collection efforts as well as an increase in the allowance for bad debts to provide for potential exposures in Europe and Latin America. Days sales in inventory decreased 12 days to 126 days at December 31, 2002 from 138 days at December 31, 2001. The lower days sales in inventory is primarily the result of improved inventory management and higher provisions for product obsolescence as a result of product launches.

The Company generated cash of $503.9 million from operations in 2002 compared with $468.3 million in 2001. The generation of cash in 2002 is the result of strong cash earnings (net earnings plus noncash adjustments) and increases in accrued expenses and income tax liabilities and decreases in the accounts receivable and inventory days mentioned previously. These items were partially offset by increases in deferred charges and accounts receivable from increased sales and payments of $8.4 million attributable to restructuring and acquisition-related liabilities and acquisition purchase liabilities. In 2002, the Company used cash of $173.6 million for business and product line acquisitions, $139.0 million for capital expenditures and $19.7 million for the payment of dividends. Business and product line acquisitions include $135.0 million paid to Tyco International Ltd. in the third quarter to acquire SDI, $14.0 million paid to Curis, Inc. to eliminate all royalties payable on future sales of OP-1 and $10.0 million paid to Pain Concepts, Inc. to acquire the DEKOMPRESSOR product line (as further discussed in Other Matters). In addition to the borrowings used to fund business and product line acquisitions, the Company borrowed an additional $438.0 million under its existing credit facilities to fund cash flow needs during 2002 and made repayments of $836.6 million against the credit facilities. Total borrowings declined by $220.9 million after adjusting for the effect of foreign currency translation.

In 2002, the Company used cash of $139.0 million for capital expenditures, including $17.9 million related to the construction of Phase II of the Company's Mahwah, New Jersey manufacturing and distribution facility. In addition, the Company spent $14.3 million for the expansion of the Company's Cork, Ireland manufacturing facility and $8.8 million for improvements to the Company's newly leased Endoscopy manufacturing facility in San Jose, California.

The Company had $37.8 million in cash and cash equivalents at December 31, 2002. The Company also had outstanding borrowings totaling $501.7 million at that date. Current maturities of long-term debt at December 31, 2002 are $10.7 million and will decrease to $0.2 million in 2004 and $0.2 million in 2005. The Company's $250.0 million 364-day revolving credit agreement expires in December 2003 and is renewable at the Company's and the lenders' discretion. The Company's $750.0 million five-year, nonamortizing, revolving credit agreement expires in December 2006. The Company believes its cash on hand as well as anticipated cash flows from operations will be sufficient to fund future operating and capital requirements and required debt repayments. Should additional funds be required, the Company had $589.8 million of additional borrowing capacity available under all of its existing credit facilities at December 31, 2002.

The Company's future contractual obligations for agreements with initial terms greater than one year are summarized as follows:

	Payment Period					
	2003	*2004*	*2005*	*2006*	*2007*	*Thereafter*
Long-term debt	$10.7	$0.2	$0.2	$487.1	$0.2	$3.3
Operating leases	40.0	31.5	22.7	16.8	13.4	45.3

The Company's additional borrowing capacity, along with the expected expiration period of the commitments, are summarized as follows:

		Amount of Commitment Expiration Per Period	
	Total Amount Committed	Less than 1 year	In excess of 1 year
Lines of credit	$581.6	$326.1	$255.5
Standby letters of credit	8.2	–	8.2

Critical Accounting Policies

The preparation of the Company's Consolidated Financial Statements requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. On an on-going basis, management evaluates these estimates. Estimates are based on historical experience, when available, and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

Management believes that an understanding of the following critical accounting policies is important in obtaining an overall understanding of the Consolidated Financial Statements.

Inventory Reserves: The Company maintains reserves for excess and obsolete inventory resulting from the potential inability to sell its products at prices in excess of current carrying costs. The markets in which the Company operates are highly competitive, with new products and surgical procedures introduced on an on-going basis. Such marketplace changes may cause the Company's products to become obsolete. The Company makes estimates regarding the future recoverability of the costs of these products and records a provision for excess and obsolete inventories based on historical experience, expiration of sterilization dates and expected future trends. If actual product life cycles, product demand or acceptance of new product introductions are less favorable than projected by management, additional inventory write-downs may be required, which could unfavorably affect future operating results.

Income Taxes: The Company operates in multiple tax jurisdictions both inside and outside the United States. Accordingly, management must determine the appropriate allocation of income in accordance with local law for each of these jurisdictions. Tax audits associated with the allocation of this income and other complex issues that may arise require an extended period of time to resolve and may result in income tax adjustments if changes to the income allocation are required between jurisdictions with different tax rates. The Company believes its income tax accruals are adequate to cover exposures related to such potential changes in income allocation between tax jurisdictions. To the extent additional information becomes available, such accruals are adjusted to reflect revised probable outcomes.

Impairment of Goodwill and Indefinite-Lived Intangibles: The Company follows the provisions of FASB Statement No. 142, *Goodwill and Other Intangible Assets,* in determining the amount, if any, by which the Company's goodwill may be impaired in value. The Company uses the two-step process prescribed in Statement No. 142. The first step is a screen for potential impairment. The second step, if necessary, measures the amount of the impairment. Inherent in the two-step process are certain assumptions and estimates necessary to determine fair values for reportable units, as defined in Statement No. 142. Should actual results or changes in future expectations differ from those projected by management, goodwill impairment charges may be required which could unfavorably affect future operating results. See Other Matters for further discussion regarding the adoption of Statement No. 142.

Other Matters

The Company distributes its products throughout the world. As a result, the Company's financial results could be significantly affected by factors such as changes in foreign currency exchange rates or weak economic conditions in foreign markets. The Company's operating results are primarily exposed to changes in exchange rates among the United States dollar and the Japanese yen and European currencies, particularly the euro and the British pound. When the United States dollar strengthens against foreign currencies, the dollar value of foreign currency sales declines. When the United States dollar weakens, the opposite situation occurs. The Company manufactures its products in the United States, France, Germany, Ireland, Switzerland, Canada and Puerto Rico and incurs the costs to manufacture in the applicable local currencies. This worldwide deployment of factories serves to partially mitigate the impact of currency exchange rate changes on the Company's cost of sales.

The Company has certain investments in net assets in international locations that are not hedged that are subject to translation gains and losses due to changes in foreign currencies. For the year ended December 31, 2002, the strengthening of foreign currencies increased the value of these investments in net assets by $79.4 million. This gain reduced the previously recorded cumulative loss from weakening of foreign currencies that is deferred and recorded as a separate component of stockholders' equity.

As of January 1, 2001, the Company adopted FASB Statement No. 133, *Accounting for Derivative Instruments and Hedging Activities,* as amended by Statements No. 137 and No. 138. The Statements require the Company to recognize all derivatives on the balance sheet at fair value. Derivatives that are not hedges must be adjusted to fair value through earnings. If a derivative is a hedge, depending on the nature of the hedge, changes in the fair value of derivatives are either offset against the change in fair value of the hedged assets, liabilities or firm commitments through earnings or recognized in accumulated other comprehensive gain (loss) until the hedged item is recognized in earnings.

The Company enters into forward currency exchange contracts to mitigate the impact of currency fluctuations on transactions denominated in nonfunctional currencies, thereby limiting risk to the Company that would otherwise result from changes in exchange rates. These nonfunctional currency exposures principally relate to intercompany payables arising from intercompany purchases of manufactured products. The periods of the forward currency exchange contracts correspond to the periods of the exposed transactions, with realized gains and losses included in the measurement and recording of transactions denominated in the nonfunctional currencies.

At December 31, 2002, the Company had outstanding forward currency exchange contracts to purchase $82.0 million and sell $97.7 million of various currencies (principally United States dollars and euros) with maturities ranging principally from 30 to 180 days. At December 31, 2001, the Company had outstanding forward currency exchange contracts to purchase $97.4 million and sell $72.1 million of various currencies (principally United States dollars and euros) with maturities ranging principally from 30 to 180 days. The estimated fair value of forward currency exchange contracts represents the measurement of the contracts at month-end spot rates as adjusted for amortized forward points. A hypothetical 10% change in exchange rates for these currencies would change the 2002 fair value by approximately $0.5 million and would have changed the 2001 fair value by approximately $1.4 million.

The Company's exposure to market risk for changes in interest rates relates to its borrowings and the accounts receivable securitization facility. The Company manages the interest rate risk on its borrowings through interest rate swap agreements, which have fixed the base rate on a $250.0 million notional amount of the $486.9 million of variable-rate borrowings outstanding at December 31, 2002. If market interest rates for similar borrowings had averaged 1% more than they did in 2002, the Company's 2002 interest expense, after considering the effects of its interest rate swaps, would have increased, and earnings before income taxes would have decreased by $1.1 million. By comparison, if market interest rates had averaged 1% less than they did during 2002, the Company's 2002 interest expense, after considering the effects of its interest rate swaps, would have decreased, and earnings before income taxes would have increased by $1.1 million. If market interest rates for the accounts receivable securitization facility had averaged 1% more than they did in 2002, the Company's discount expense would have increased, and earnings before income taxes would have decreased by $1.3 million. By comparison, if market interest rates

had averaged 1% less than they did in 2002, the Company's discount expense would have decreased, and earnings before income taxes would have increased by $1.3 million. These amounts are determined by considering the impact of hypothetical interest rates on the Company's borrowing cost, interest rate swap agreements and accounts receivable securitization facility without any actions by management to mitigate its exposure to such changes.

The Company is exposed to credit loss in the event of nonperformance by counterparties on the above instruments, but does not anticipate nonperformance by any of the counterparties.

The Company's interest rate swap agreements effectively convert a portion of its variable-rate borrowings to a fixed-rate basis through 2003, thus reducing the impact of changes in interest rates on future interest expense. Approximately 51% of the Company's outstanding variable-rate borrowings as of December 31, 2002 have been hedged through the designation of interest rate swap agreements classified as cash flow hedges. A gain of $9.3 million attributable to changes in the fair value of interest rate swap agreements was recorded as a component of accumulated other comprehensive gain (loss) in 2002. If in the future the interest rate swap agreements were determined to be ineffective or were terminated before the contractual termination dates, or if it became probable that the hedged variable cash flows associated with the variable-rate borrowings would stop, the Company would be required to reclassify into earnings all or a portion of the unrealized losses on cash flow hedges included in accumulated other comprehensive gain (loss). Interest rate differentials to be paid or received as a result of interest rate swaps are recognized as an adjustment of interest expense related to the designated borrowings. Based on the maturities of the Company's interest rate swap agreements, interest expense for the year ending December 31, 2003 is expected to be $9.2 million higher than the interest cost on the variable-rate borrowings through the recognition of amounts included as unrealized losses on cash flow hedges at December 31, 2002.

The Company uses yen-denominated floating-rate borrowings to protect a portion of the value of its investment in its subsidiary in Japan. Realized and unrealized gains and losses from this hedge are not included in the Consolidated Statements of Earnings, but are recorded as foreign currency translation adjustments within accumulated other comprehensive gain (loss) in stockholders' equity. Net gains (losses) of ($1.6) million, $5.8 million and $7.7 million attributable to the yen-denominated floating-rate borrowings hedge were recorded as foreign currency translation adjustments in 2002, 2001 and 2000, respectively.

As of January 1, 2002, the Company adopted the provisions of FASB Statement No. 142, *Goodwill and Other Intangible Assets,* related to acquisitions completed before July 1, 2001. Statement No. 142 prohibits the amortization of goodwill and intangible assets with indefinite lives and requires the Company to evaluate these intangibles for impairment on an annual basis. In accordance with the Statement's provisions, an assembled workforce intangible asset with an unamortized balance of $5.5 million as of January 1, 2002 was reclassified from other intangibles to goodwill. In the first quarter of 2002, the Company completed the initial impairment test of goodwill and, in the fourth quarter of 2002, completed the required annual impairment test of goodwill as prescribed by Statement No. 142, and determined that recorded goodwill was not impaired and no goodwill write-down was necessary.

In October 2002, the Company purchased the DEKOMPRESSOR product line from Pain Concepts, Inc., at a total cost of $10.0 million giving the Company access to intellectual property and other commercial rights relating to the design and manufacture of certain medical devices. Intangible assets acquired, principally patents, are being amortized over 17 years. The Company is contingently liable for potential future milestone payments of up to $42.5 million, primarily based on future sales growth over the next five years.

On October 1, 2002, the Company entered into an agreement with Curis, Inc., which eliminated all royalties payable to Curis relating to future Stryker sales of OP-1. Under terms of the agreement, the Company made a one-time cash payment of $14.0 million to Curis. The payment was allocated to existing patents and is being amortized over 15 years.

On July 1, 2002, the Company acquired SDI from Tyco International Ltd., for $135.0 million in cash. The acquisition expands the Company's spinal product line by adding interbody spinal cages for the United States market as well as other thoracolumbar and cervical spinal fixation devices. The acquisition was funded using existing credit facilities.

The acquisition of SDI was accounted for using the purchase method of accounting. The results of operations for the acquired business are included in the Company's Consolidated Financial Statements beginning July 1, 2002. The acquisition of SDI added $25.3 million to the Company's sales for the second half of 2002. SDI had sales of $55.6 million for the year ended December 31, 2001 and sales of $33.1 million for the six months ended June 30, 2002. The purchase price of $135.0 million in cash and liabilities assumed has been preliminarily allocated to the assets acquired and liabilities assumed based on their estimated fair value at the date of acquisition. Based on the preliminary purchase price allocation, $87.1 million of the purchase price was allocated to patent licensing agreements to be amortized over their remaining life of 8 years, $12.4 million to inventory, $38.0 million to deferred tax assets related to future tax deductions, $5.1 million to other tangible assets and $7.6 million to liabilities assumed. Immediately after the acquisition was consummated, management of the Company began to implement an integration plan to combine Stryker and SDI. In conjunction with the integration plan, the Company has recorded additional purchase liabilities of $3.6 million, which were included in the preliminary purchase price allocation. The additional purchase liabilities include $3.1 million for severance and related costs and $0.5 million for contractual obligations. The severance and related costs are provided for workforce reductions covering 37 SDI employees. The workforce reductions were completed during the fourth quarter of 2002 with severance payments to be made through the third quarter of 2003. The Company's pro forma consolidated financial results did not differ significantly as a result of the SDI acquisition.

In July 2002, the FASB issued Statement No. 146, *Accounting for Costs Associated with Exit or Disposal Activities.* The Statement addresses the timing of recognition and the related measurement of the costs of one-time termination benefits such as those associated with the closing of the Rutherford facility. Under the provisions of Statement No. 146, the employment-related closing costs for Rutherford would be recognized over the 12-month closing period. Statement No. 146 is effective for exit activities initiated after December 31, 2002, with early application allowed. The Company initiated the actions related to Rutherford in June 2002 and did not adopt the provisions of Statement No. 146 when recording the costs of the Rutherford closing. Accordingly, the actual employment-related costs of the closing were expensed, upon union approval of the shutdown agreement, in the third quarter of 2002.

In November 2002, the FASB issued Interpretation No. 45, *Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others.* Interpretation No. 45 changes current practice in accounting for, and disclosure of, guarantees. Interpretation No. 45 will require that certain guarantees be recorded as liabilities at fair value on the Company's balance sheet. Current practice requires that liabilities related to guarantees be recorded only when a loss is probable and reasonably estimable, as those terms are defined in FASB Statement No. 5, *Accounting for Contingencies.* Interpretation No. 45 also requires a guarantor to make significant new disclosures, even when the likelihood of making any payments under the guarantee is remote, which is another change from current practice. The disclosure requirements of Interpretation No. 45 are effective immediately and are included in Note 14, "Contingencies" to the Consolidated Financial Statements. The initial recognition and measurement provisions are applicable on a prospective basis to guarantees issued or modified after December 31, 2002. The Company has not yet determined what effect, if any, the new recognition and measurement provisions will have on the Company's future financial results.

In December 2002, the FASB issued Statement No. 148, *Accounting for Stock-Based Compensation—Transition and Disclosure—an amendment of FASB Statement No. 123.* Statement No. 148 amends Statement No. 123, *Accounting for Stock-Based Compensation,* to provide alternative methods of transition for a voluntary change to the fair-value based method of accounting for stock-based employee compensation. In addition, Statement No. 148 amends the disclosure requirements of Statement No. 123 to require disclosure in interim financial statements regarding the method of accounting for stock-based employee compensation and the effect of the method used on reported results. The Company does not intend to adopt a fair-value based method of accounting for stock-based employee compensation until a final standard is issued by the FASB that addresses concerns related to applicability of current option pricing models to non-exchange traded employee stock option plans.

Forward-Looking Statements

The information contained in this report may contain information that includes or is based on forward-looking statements within the meaning of the federal securities laws that are subject to risks and uncertainties. These statements may be identified by the use of words such as "anticipates," "expects," "estimates," "projects," "intends" and "believes" and variations thereof and other terms of similar meaning. Factors that could cause the Company's actual results and financial condition to differ from the Company's expectations include, but are not limited to: regulatory actions, including cost-containment measures, that could adversely affect the price of or demand for the Company's products; changes in reimbursement levels from third-party payors; a significant increase in product liability claims; changes in economic conditions that adversely affect the level of demand for the Company's products; changes in foreign exchange markets; changes in financial markets; and changes in the competitive environment.

While the Company believes that the assumptions underlying such forward-looking statements are reasonable, there can be no assurance that future events or developments will not cause such statements to be inaccurate. All forward-looking statements contained in this report are qualified in their entirety by this cautionary statement.

CONSOLIDATED BALANCE SHEETS Stryker Corporation and Subsidiaries

(in millions, except per share amounts)

	December 31	
	2002	*2001*
ASSETS		
Current Assets		
Cash and cash equivalents	$37.8	$50.1
Accounts receivable, less allowance of $43.7 ($36.3 in 2001)	406.7	332.1
Inventories	426.5	399.8
Deferred income taxes	227.5	171.5
Prepaid expenses and other current assets	52.8	39.6
Total current assets	1,151.3	993.1
Property, Plant and Equipment		
Land, buildings and improvements	333.4	287.6
Machinery and equipment	591.3	469.3
	924.7	756.9
Less allowance for depreciation	405.5	312.9
	519.2	444.0
Other Assets		
Goodwill, less accumulated amortization of $64.8 ($58.5 in 2001)	460.0	434.3
Other intangibles, less accumulated amortization of $99.3 ($74.5 in 2001)	475.1	368.0
Deferred charges, less accumulated amortization of $274.1 ($205.5 in 2001)	123.7	102.1
Deferred income taxes	61.8	60.4
Other	24.4	21.7
	1,145.0	986.5
	$2,815.5	$2,423.6
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current Liabilities		
Accounts payable	$106.0	$108.5
Accrued compensation	161.4	128.5
Restructuring and acquisition-related liabilities	25.5	13.3
Income taxes	133.2	75.1
Accrued expenses and other liabilities	270.7	206.3
Current maturities of long-term debt	10.7	1.7
Total current liabilities	707.5	533.4
Long-Term Debt, Excluding Current Maturities	491.0	720.9
Other Liabilities	118.8	113.1
Stockholders' Equity		
Common stock, $.10 par value:		
Authorized—500.0 shares		
Outstanding—198.1 shares (196.7 in 2001)	19.8	19.7
Additional paid-in capital	120.7	83.2
Retained earnings	1,442.6	1,120.7
Accumulated other comprehensive loss	(84.9)	(167.4)
Total stockholders' equity	1,498.2	1,056.2
	$2,815.5	$2,423.6

See accompanying notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF EARNINGS Stryker Corporation and Subsidiaries

(in millions, except per share amounts)

	Years ended December 31		
	2002	*2001*	*2000*
Net sales	$3,011.6	$2,602.3	$2,289.4
Cost of sales	1,111.2	963.8	815.2
Gross profit	1,900.4	1,638.5	1,474.2
Research, development and engineering expenses	141.4	142.1	122.2
Selling, general and administrative expenses	1,165.4	985.4	885.6
Restructuring and acquisition-related items	17.2	0.6	(1.0)
	1,324.0	1,128.1	1,006.8
Other expense (income):			
Interest expense	40.3	67.9	96.6
Intangibles amortization	28.9	38.4	34.7
Other	0.5	(1.6)	1.2
	69.7	104.7	132.5
Earnings before income taxes and extraordinary item	506.7	405.7	334.9
Income taxes	161.1	133.9	113.9
Earnings before extraordinary item	345.6	271.8	221.0
Extraordinary loss, net of income taxes	–	(4.8)	–
Net earnings	$345.6	$267.0	$221.0
Basic earnings per share of common stock:			
Before extraordinary item	$1.75	$1.38	$1.13
Extraordinary loss	–	($.02)	–
Net earnings	$1.75	$1.36	$1.13
Diluted earnings per share of common stock:			
Before extraordinary item	$1.70	$1.34	$1.10
Extraordinary loss	–	($.02)	–
Net earnings	$1.70	$1.32	$1.10

See accompanying notes to consolidated financial statements.

(in millions, except per share amounts)

	Common Stock	Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Gain (Loss)	Total
Balances at January 1, 2000	$19.4	$27.1	$668.1	($43.1)	$671.5
Net earnings for 2000	–	–	221.0	–	221.0
Unrealized losses on securities of $0.4 (net of $0.1 income tax benefit), net of reclassification adjustment for gains included in net earnings	–	–	–	(0.5)	(0.5)
Foreign currency translation adjustments	–	–	–	(58.8)	(58.8)
Comprehensive earnings for 2000	–	–	–	–	161.7
Issuance of 1.1 shares of common stock under stock option and benefit plans, including $13.8 income tax benefit	0.1	17.5	–	–	17.6
Common stock issued in business acquisitions	0.1	19.7	–	–	19.8
Cash dividend declared of $.08 per share of common stock	–	–	(15.7)	–	(15.7)
Balances at December 31, 2000	19.6	64.3	873.4	(102.4)	854.9
Cumulative effect of accounting change related to cash flow hedges	–	–	–	3.5	3.5
Net earnings for 2001	–	–	267.0	–	267.0
Unrealized losses on securities of $0.2, net of $0.1 income tax benefit	–	–	–	(0.1)	(0.1)
Unrealized losses related to cash flow hedges	–	–	–	(22.0)	(22.0)
Foreign currency translation adjustments	–	–	–	(46.4)	(46.4)
Comprehensive earnings for 2001	–	–	–	–	198.5
Issuance of 0.8 shares of common stock under stock option and benefit plans, including $10.4 income tax benefit	0.1	18.9	–	–	19.0
Cash dividend declared of $.10 per share of common stock	–	–	(19.7)	–	(19.7)
Balances at December 31, 2001	19.7	83.2	1,120.7	(167.4)	1,056.2
Net earnings for 2002	–	–	345.6	–	345.6
Unrealized gains on securities of $0.3, net of $0.1 income tax expense	–	–	–	0.2	0.2
Unrealized gains related to cash flow hedges	–	–	–	9.3	9.3
Unfunded pension losses, net of $3.4 income tax benefit	–	–	–	(6.4)	(6.4)
Foreign currency translation adjustments	–	–	–	79.4	79.4
Comprehensive earnings for 2002	–	–	–	–	428.1
Issuance of 1.4 shares of common stock under stock option and benefit plans, including $22.5 income tax benefit	0.1	37.5	–	–	37.6
Cash dividend declared of $.12 per share of common stock	–	–	(23.7)	–	(23.7)
Balances at December 31, 2002	$19.8	$120.7	$1,442.6	($84.9)	$1,498.2

See accompanying notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS Stryker Corporation and Subsidiaries

(in millions)

	Years ended December 31		
	2002	*2001*	*2000*
Operating Activities			
Net earnings	$345.6	$267.0	$221.0
Adjustments to reconcile net earnings to net cash provided by operating activities:			
Depreciation	86.3	74.5	74.7
Amortization	99.8	97.5	93.9
Write-off of unamortized deferred loan costs	–	7.1	–
Restructuring and acquisition-related items	17.2	0.6	(1.0)
Payments of restructuring and acquisition-related liabilities	(4.9)	(3.7)	(7.3)
Provision for losses on accounts receivable	16.0	16.9	7.2
Deferred income taxes (credit)	(1.8)	29.1	28.7
Other	1.9	9.2	8.0
Changes in operating assets and liabilities, net of effects of business and product line acquisitions:			
Proceeds from accounts receivable securitization	–	2.7	30.3
Accounts receivable	(64.4)	(23.8)	(24.6)
Inventories	7.0	(10.2)	(20.2)
Deferred charges	(84.6)	(65.1)	(68.2)
Accounts payable	(3.2)	9.8	(15.2)
Payments of acquisition purchase liabilities	(3.5)	(7.5)	(30.1)
Accrued expenses	75.6	40.2	49.3
Income taxes	26.9	27.9	(7.1)
Other	(10.0)	(3.9)	(7.6)
Net cash provided by operating activities	503.9	468.3	331.8
Investing Activities			
Business and product line acquisitions, net of cash acquired	(173.6)	(43.0)	(24.5)
Proceeds from sales of property, plant and equipment	0.8	9.0	4.8
Purchases of property, plant and equipment	(139.0)	(161.9)	(80.7)
Sales and maturities of marketable securities	–	–	7.1
Net cash used in investing activities	(311.8)	(195.9)	(93.3)
Financing Activities			
Proceeds from borrowings	611.6	935.8	209.9
Payments on borrowings	(836.6)	(1,211.4)	(463.3)
Dividends paid	(19.7)	(15.7)	(12.7)
Proceeds from exercise of stock options	32.0	14.7	14.2
Other	0.1	(1.0)	(6.8)
Net cash used in financing activities	(212.6)	(277.6)	(258.7)
Effect of exchange rate changes on cash and cash equivalents	8.2	1.3	(5.8)
Decrease in cash and cash equivalents	(12.3)	(3.9)	(26.0)
Cash and cash equivalents at beginning of year	50.1	54.0	80.0
Cash and cash equivalents at end of year	$37.8	$50.1	$54.0

See accompanying notes to consolidated financial statements.

NOTE 1
SIGNIFICANT ACCOUNTING POLICIES

Business: Stryker Corporation develops, manufactures and markets specialty surgical and medical products that are sold primarily to hospitals throughout the world and provides outpatient physical therapy services in the United States.
Principles of Consolidation: The Consolidated Financial Statements include the accounts of the Company and its majority-owned subsidiaries after elimination of all significant intercompany accounts and transactions.
Revenue Recognition: Revenue is recognized on the sale of products and services when the related goods have been shipped and title passes or services have been rendered.
Shipping and Handling of Products: Amounts billed to customers for shipping and handling of products are included in net sales in 2002 and 2001. Prior to 2001, such amounts were recorded as an offset to cost of sales. Costs incurred related to shipping and handling of products are included in cost of sales in 2002 and 2001. Prior to 2001, certain shipping costs were reported in selling, general and administrative expenses.
Use of Estimates: The preparation of these Consolidated Financial Statements in conformity with generally accepted accounting principles requires Company management to make estimates and assumptions that affect the amounts reported in the Consolidated Financial Statements and accompanying notes. Actual results could differ from those estimates.
Foreign Currency Translation: The functional currencies for the Company's international affiliates are their local currencies. Accordingly, the financial statements of the Company's international affiliates are translated into United States dollars using current exchange rates for balance sheets and average exchange rates for statements of earnings and cash flows. Unrealized translation adjustments are included in accumulated other comprehensive gain (loss) in stockholders' equity. Transaction gains and losses, such as those resulting from the settlement of nonfunctional currency receivables or payables, are included in net earnings.
Cash Equivalents and Investments: Cash equivalents are highly liquid investments with a maturity of three months or less when purchased. Investments include marketable equity securities and other investments classified in other assets. Other investments consist of mutual funds that are acquired to offset changes in certain liabilities related to deferred compensation arrangements.

The Company's investments are stated at fair value based on quoted market prices. Interest, dividends and realized gains and losses on the sale of cash equivalents and marketable equity securities are included in other expense (income). Adjustments to the fair value of marketable equity securities, which are classified as available-for-sale, are recorded as increases or decreases, net of income taxes, within accumulated other comprehensive gain (loss) in stockholders' equity. Adjustments to the fair value of other investments, which are classified as trading, are recorded in earnings as offsets to the related changes in liabilities under deferred compensation arrangements.
Accounts Receivable Securitization: The Company has an accounts receivable securitization facility pursuant to which certain subsidiaries of the Company sell on an ongoing basis all of their domestic accounts receivable to Stryker Funding Corporation, a wholly owned special-purpose subsidiary of the Company, which in turn may sell up to an aggregate of a $130.0 undivided percentage ownership interest in such receivables to a multiseller commercial paper conduit administered by a bank. Creditors of Stryker Funding Corporation have a claim to its assets before any equity becomes available to the Company.

The amounts of accounts receivable sold to Stryker Funding Corporation, net of the Company's retained interest, totaled $130.0 at December 31, 2002 and 2001, and are reflected in the balance sheet as reductions of accounts receivable. The amount of receivables sold is subject to change monthly, based on the level of defined eligible receivables less contractual reserves. The Company's retained interest in accounts receivable held by Stryker Funding Corporation, which is in the form of a subordinated note, represents an overcollateralization of the undivided interest sold. This retained interest totaled $98.5 and $76.8 at December 31, 2002 and 2001, respectively. Discount expense associated with the securitization facility, including the conduit's financing cost of issuing its commercial paper, was $2.7 in 2002, $5.8 in 2001 and $7.1 in 2000 and is included in selling, general and administrative expenses.

Inventories: Inventories are stated at the lower of cost or market. Cost for approximately 88% (87% in 2001) of inventories is determined using the lower of first-in, first-out (FIFO) cost or market. Cost for certain domestic inventories is determined using the last-in, first-out (LIFO) cost method. The FIFO cost for all inventories approximates replacement cost.

The Company maintains reserves for excess and obsolete inventory resulting from the potential inability to sell its products at prices in excess of current carrying costs. The markets in which the Company operates are highly competitive, with new products and surgical procedures introduced on an on-going basis. Such marketplace changes may cause the Company's products to become obsolete. The Company makes estimates regarding the future recoverability of the cost of these products and records a provision for excess and obsolete inventories based on historical experience, expiration of sterilization dates and expected future trends.

Property, Plant and Equipment: Property, plant and equipment is stated at cost. Depreciation is computed by either the straight-line or declining-balance method over the estimated useful lives of 3 to 30 years for buildings and improvements and 3 to 10 years for machinery and equipment.

Goodwill and Other Intangible Assets: Goodwill represents the excess of purchase price over fair value of tangible net assets of acquired businesses after amounts allocated to other intangible assets. Other intangible assets include developed technology, which is amortized on a straight-line basis over 20 years, and customer relationships (which reflect expected continued customer patronage), trademarks, trade names and patents, which are amortized on a straight-line basis over 5 to 35 years (weighted average life of 15 years for other intangible assets).

Deferred Charges: Deferred charges represent the net book value of loaner instruments for surgical implants provided to customers by the Company. These instruments are amortized on a straight-line basis over a three-year period. Amortization expenses for instruments are included in selling, general and administrative expenses.

Deferred Loan Costs: Deferred loan costs associated with the Company's borrowings are amortized over the terms of the related borrowings using the effective-interest method. Deferred loan costs are classified in other assets and had a net book value of $2.5 and $2.9 at December 31, 2002 and 2001, respectively. Amortization expenses for deferred loan costs are included in interest expense and were $0.6 in 2002, $5.9 in 2001 and $8.2 in 2000. The prepayment of the remaining amounts outstanding under the Company's Senior Secured Credit Facilities in December 2001 resulted in the write-off of related unamortized deferred loan costs of $7.1 (see Note 7).

Income Taxes: The Company accounts for income taxes using the liability method. Under this method, deferred tax assets and liabilities are determined based on differences between financial reporting and tax bases of assets and liabilities and are measured using the enacted tax rates in effect for the years in which the differences are expected to reverse. Deferred income tax expense (credit) represents the change in net deferred tax assets and liabilities during the year.

Derivative Financial Instruments: The Company uses derivative financial instruments to manage the economic impact of fluctuations in interest rates and currency exchange rates. The Company enters into interest rate swaps and currency forward contracts to manage these economic risks.

As of January 1, 2001, the Company adopted Financial Accounting Standards Board (FASB) Statement No. 133, *Accounting for Derivative Instruments and Hedging Activities,* as amended by Statements No. 137 and No. 138. The Statements require the Company to recognize all derivatives on the balance sheet at fair value. Derivatives that are not hedges must be adjusted to fair value through earnings. If a derivative is a hedge, depending on the nature of the hedge, changes in the fair value of derivatives are either offset against the change in fair value of the hedged assets, liabilities or firm commitments through earnings or recognized in accumulated other comprehensive gain (loss) until the hedged item is recognized in earnings (see Note 2).

Legal and Other Contingencies: The Company is involved in various proceedings, legal actions and claims arising in the normal course of business, including proceedings related to product, labor and other matters. The potential future outcomes of these matters are outside of management's complete control and 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 relief, which could result in the payment of significant claims and settlements. In legal matters for which management has sufficient information to reasonably estimate the Company's future obligations, a liability representing management's best estimate of the probable cost for the resolution of these legal matters is recorded. The estimates are based on consultation with outside counsel, previous settlement experience and settlement strategies.

Stock Options: At December 31, 2002, the Company has key employee and director stock option plans, which are described more fully in Note 8. The Company follows Accounting Principles Board (APB) Opinion No. 25, *Accounting for Stock Issued to Employees,* in accounting for its stock option plans. Under Opinion No. 25, no compensation expense is recognized because the exercise price of the Company's stock options equals the market price of the underlying stock on the date of grant. Had compensation expense for the Company's stock-based compensation plans been determined based on the fair value at the grant dates for awards under those plans consistent with the method of FASB Statement No. 123, *Accounting for Stock-Based Compensation,* the Company's net earnings and net earnings per share would have been as follows:

	2002	*2001*	*2000*
Net earnings:			
As reported	$345.6	$267.0	$221.0
Deduct: Compensation expense—fair value method	(17.1)	(11.8)	(9.9)
Pro forma	$328.5	$255.2	$211.1
Basic net earnings per share:			
As reported	$1.75	$1.36	$1.13
Pro forma	$1.66	$1.30	$1.08
Diluted net earnings per share:			
As reported	$1.70	$1.32	$1.10
Pro forma	$1.61	$1.26	$1.05

The weighted-average fair value per share of options granted during 2002, 2001 and 2000, estimated on the date of grant using the Black-Scholes option pricing model, was $22.94, $21.76 and $14.82, respectively. The fair value of options granted was estimated on the date of grant using the following assumptions:

	2002	*2001*	*2000*
Risk-free interest rate	3.76%	4.99%	5.17%
Expected dividend yield	0.18%	0.15%	0.26%
Expected stock price volatility	37.4%	38.0%	37.0%
Expected option life	6.5 years	6.6 years	6.5 years

Comprehensive Gain (Loss): The components of accumulated other comprehensive gain (loss) are as follows:

	Unrealized Gains (Losses) on Securities	Unrealized Gains (Losses) on Cash Flow Hedges	Unfunded Pension Losses	Foreign Currency Translation Adjustments	Accumulated Other Comprehensive Gain (Loss)
Balances at January 1, 2001	($0.8)	–	–	($101.6)	($102.4)
Cumulative effect of accounting change related to cash flow hedges	–	$3.5	–	–	3.5
Other comprehensive loss for 2001	(0.1)	(22.0)	–	(46.4)	(68.5)
Balances at December 31, 2001	(0.9)	(18.5)	–	(148.0)	(167.4)
Other comprehensive gain (loss) for 2002	0.2	9.3	($6.4)	79.4	82.5
Balances at December 31, 2002	($0.7)	($9.2)	($6.4)	($68.6)	($84.9)

Recently Issued Accounting Standards: In July 2002, the FASB issued Statement No. 146, *Accounting for Costs Associated with Exit or Disposal Activities.* Statement No. 146 addresses the timing of recognition and the related measurement of the costs of one-time termination benefits such as those associated with the closing of the Rutherford facility. Under the provisions of Statement No. 146, the employment-related closing costs for Rutherford would be recognized over the 12-month closing period. Statement No. 146 is effective for exit activities initiated after December 31, 2002, with early application allowed. The Company initiated the actions related to Rutherford in June 2002 and did not adopt the provisions of Statement No. 146 when recording the costs of the Rutherford closing. Accordingly, the actual employment-related costs of the closing were expensed, upon approval of the shutdown agreement, in the third quarter of 2002. See Note 6, "Restructuring and Acquisition-Related Liabilities," for further information regarding the Rutherford closing.

In November 2002, the FASB issued Interpretation No. 45, *Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others.* Interpretation No. 45 changes current practice in accounting for, and disclosure of, guarantees. Interpretation No. 45 will require certain guarantees to be recorded as liabilities at fair value on the Company's balance sheet. Current practice requires that liabilities related to guarantees be recorded only when a loss is probable and reasonably estimable, as those terms are defined in FASB Statement No. 5, *Accounting for Contingencies.* Interpretation No. 45 also requires a guarantor to make significant new disclosures, even when the likelihood of making any payments under the guarantee is remote, which is another change from current practice. The disclosure requirements of Interpretation No. 45 are effective immediately and are included in Note 14, "Contingencies." The initial recognition and measurement provisions are applicable on a prospective basis to guarantees issued or modified after December 31, 2002. The Company has not yet determined what effect, if any, the new recognition and measurement provisions will have on the Company's future financial results.

In December 2002, the FASB issued Statement No. 148, *Accounting for Stock-Based Compensation—Transition and Disclosure—an amendment of FASB Statement No. 123.* Statement No. 148 amends Statement No. 123, *Accounting for Stock-Based Compensation,* to provide alternative methods of transition for a voluntary change to the fair-value based method of accounting for stock-based employee compensation. In addition, Statement No. 148 amends the disclosure requirements of Statement No. 123 to require disclosure in interim financial statements regarding the method of accounting for stock-based employee compensation and the effect of the method used on reported results. The Company does not intend to adopt a fair-value based method of accounting for stock-based employee compensation until a final standard is issued by the FASB that addresses concerns related to the applicability of current option pricing models to non-exchange traded employee stock option plans.

Reclassifications: Certain prior year amounts have been reclassified to conform with the presentation used in 2002.

NOTE 2
FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

The following is a summary of the Company's investments:

	Cost	Gross Unrealized Losses	Estimated Fair Value
At December 31, 2002:			
Equity securities	$2.6	($1.1)	$1.5
Other investments	11.3	–	11.3
Total	$13.9	($1.1)	$12.8
At December 31, 2001:			
Equity securities	$2.6	($1.4)	$1.2
Other investments	9.3	–	9.3
Total	$11.9	($1.4)	$10.5

Net realized losses on sales of the Company's investments in 2002 and 2001 totaled $0.1 and $0.9, respectively. Net realized gains on sales of the Company's investments totaled $3.3 in 2000.

Interest income, which is included in other income, totaled $2.4 in 2002, $2.2 in 2001 and $4.1 in 2000.

The Company enters into forward currency exchange contracts to mitigate the impact of currency fluctuations on transactions denominated in nonfunctional currencies, thereby limiting risk to the Company that would otherwise result from changes in exchange rates. These nonfunctional currency exposures relate principally to intercompany receivables and payables arising from intercompany purchases of manufactured products. The periods of the forward currency exchange contracts correspond to the periods of the exposed transactions, with realized gains and losses included in the measurement and recording of transactions denominated in the nonfunctional currencies. All currency forward contracts and cross-currency swaps are marked-to-market each period with resulting gains (losses) included in other expense (income) in the Consolidated Statements of Earnings.

At December 31, 2002, the Company had outstanding forward currency exchange contracts to purchase $82.0 and sell $97.7 of various currencies (principally United States dollars and euros) with maturities ranging principally from 30 to 180 days. At December 31, 2001, the Company had outstanding forward currency exchange contracts to purchase $97.4 and sell $72.1 of various currencies (principally United States dollars and euros) with maturities ranging principally from 30 to 180 days. The estimated fair value of forward currency exchange contracts represents the measurement of the contracts at month-end spot rates as adjusted for amortized forward points.

The Company has entered into interest rate swap agreements that effectively convert a portion of its variable-rate borrowings to a fixed-rate basis through 2003, thus reducing the impact of changes in interest rates on future interest expense. Approximately 51% of the Company's outstanding variable-rate borrowings as of December 31, 2002 have been hedged through the designation of interest rate swap agreements classified as cash flow hedges. The Company has fixed the base rate on a $250.0 notional amount of the $486.9 of variable-rate borrowings outstanding at December 31, 2002 at an average rate of 5.58%. The interest rate swaps mature over various terms ranging from September 2003 through December 2003. The fair value of the Company's interest rate swap agreements represents the estimated receipts or payments that would be made to terminate the agreements.

Upon adoption of FASB Statement No. 133, as amended, on January 1, 2001 the Company recognized a gain from the cumulative effect of an accounting change of $3.5 in accumulated other comprehensive gain (loss) related to the interest rate swap agreements. A gain of $9.3 and a loss of $22.0 attributable to changes in the fair value of interest rate swap agreements was recorded as a component of accumulated other comprehensive gain (loss) in 2002 and 2001, respectively. If in the future the interest rate swap agreements were determined to be ineffective or were terminated before the contractual termination dates, or if it became probable that the hedged variable cash flows associated with the variable-rate borrowings would stop, the Company would be required to reclassify into earnings all or a portion of the unrealized losses on cash flow hedges included in accumulated other comprehensive gain (loss). Interest rate differentials to be paid or received as a result of interest rate swaps are recognized as an adjustment of interest expense related to the designated borrowings. Based on the maturities of the Company's interest rate swap agreements, interest expense for the year ending December 31, 2003 is expected to be $9.2 higher than the interest cost on the variable-rate borrowings through the recognition of amounts included as unrealized losses on cash flow hedges at December 31, 2002.

The Company uses yen-denominated floating-rate borrowings to protect a portion of the value of its investment in its subsidiary in Japan. Realized and unrealized gains and losses from this hedge are not included in the Consolidated Statements of Earnings, but are recorded as foreign currency translation adjustments within accumulated other comprehensive gain (loss) in stockholders' equity. Net gains (losses) of ($1.6), $5.8 and $7.7 attributable to the yen-denominated floating-rate borrowings hedge were recorded as foreign currency translation adjustments in 2002, 2001 and 2000, respectively.

The Company is exposed to credit loss in the event of nonperformance by counterparties on the above instruments but does not anticipate nonperformance by any of the counterparties.

NOTE 3
INVENTORIES

Inventories are summarized as follows:

	December 31	
	2002	*2001*
Finished goods	$319.2	$306.9
Work-in-process	51.8	38.6
Raw material	60.7	61.6
FIFO cost	431.7	407.1
Less LIFO reserve	5.2	7.3
	$426.5	$399.8

NOTE 4
BUSINESS AND PRODUCT LINE ACQUISITIONS

In October 2002, the Company purchased the DEKOMPRESSOR product line from Pain Concepts, Inc., at a total cost of $10.0 giving the Company access to intellectual property and other commercial rights relating to the design and manufacture of certain medical devices. Intangible assets acquired are being amortized over 17 years. The Company is contingently liable for potential future milestone payments of up to $42.5, primarily based on future sales growth over the next five years.

On October 1, 2002, the Company entered into an agreement with Curis, Inc., which eliminated all royalties payable to Curis relating to future Stryker sales of osteogenic protein-1 (OP-1). Under terms of the agreement, the Company made a one-time cash payment of $14.0 to Curis. The payment was allocated to existing patents and is being amortized over 15 years.

On July 1, 2002, the Company acquired the Surgical Dynamics Inc. spinal implant business (SDI) from Tyco International Ltd. for $135.0 in cash. The acquisition expands the Company's spinal product line by adding interbody spinal cages for the United States market as well as other thoracolumbar and cervical spinal fixation devices. The acquisition was funded using existing credit facilities.

The acquisition of SDI was accounted for using the purchase method of accounting. The results of operations for the acquired business are included in the Company's Consolidated Financial Statements beginning July 1, 2002. The acquisition of SDI added $25.3 to the Company's sales for the second half of 2002. SDI had sales of $55.6 for the year ended December 31, 2001 and sales of $33.1 for the six months ended June 30, 2002. The purchase price of $135.0 in cash and liabilities assumed has been preliminarily allocated to the assets acquired and liabilities assumed based on their estimated fair value at the date of acquisition. Based on the preliminary purchase price allocation, $87.1 of the purchase price was allocated to patent licensing agreements to be amortized over their remaining life of 8 years, $12.4 to inventory, $38.0 to deferred tax assets related to future tax deductions, $5.1 to other tangible assets, and $7.6 to liabilities assumed. Immediately after the acquisition was consummated, management of the Company began to implement an integration plan to combine Stryker and SDI. In conjunction with the integration plan, the Company has recorded additional purchase liabilities of $3.6, which were included in the preliminary purchase price allocation. The additional purchase liabilities include $3.1 for severance and related costs and $0.5 for contractual obligations. The severance and related costs are provided for workforce reductions covering 37 SDI employees. The workforce reductions were completed during the fourth quarter of 2002 with severance payments to be made through the third quarter of 2003. Pro forma consolidated results of operations would not differ significantly as a result of the SDI acquisition.

In November 2001, the Company acquired the business of an independent Italian distributor of certain of the Company's products at a cost of approximately euro 28.2 ($25.3). An initial cash payment of euro 7.3 ($6.5) was made in November 2001, with the remaining purchase price to be paid ratably over a five-year period. The purchase consolidates the distribution of substantially all of the Company's products in Italy. The acquisition was accounted for using the purchase method of accounting. Tangible assets acquired included $5.1 of inventory and $0.8 of deferred charges. Intangible assets acquired principally included customer relationships and noncompete agreements. Approximately $10.2 of the purchase price was allocated to customer relationships and is being amortized over 20 years. Approximately $9.2 of the purchase price was allocated to other intangibles, principally noncompete agreements, and is being amortized over a weighted average life of four years.

In August 2000, the Company completed the acquisition of Image Guided Technologies, Inc. (IGT) by merger for 0.3 shares of Stryker common stock with a value of $12.0. IGT manufactured three-dimensional optical measurement devices ("optical localizers") for anatomical image-display workstations used by physicians to perform image-guided surgery. The acquisition was accounted for using the purchase method of accounting. Intangible assets acquired, principally patents, are being amortized over periods ranging from 10 to 15 years.

NOTE 5
GOODWILL AND OTHER INTANGIBLE ASSETS

As of January 1, 2002, the Company adopted the provisions of FASB Statement No. 142, *Goodwill and Other Intangible Assets,* related to acquisitions completed before July 1, 2001. Statement No. 142 prohibits the amortization of goodwill and intangible assets with indefinite lives and requires the Company to evaluate these intangibles for impairment on an annual basis. In accordance with the Statement's provisions, an assembled workforce intangible asset with an unamortized balance of $5.5 as of January 1, 2002 was reclassified from other intangibles to goodwill. In the first quarter of 2002, the Company completed the required impairment test of goodwill and, in the fourth quarter of 2002, completed the required annual impairment test of goodwill as prescribed by Statement No. 142 and determined that recorded goodwill was not impaired and that no goodwill write-down was necessary.

If the nonamortization provisions of Statement No. 142 had been applied in 2001 and 2000, amortization expense would have been reduced by $18.1 ($12.1 net of income taxes) and $17.3 ($11.5 net of income taxes), respectively. Reconciliations of reported net earnings to adjusted net earnings for 2001 and 2000 are presented to show what net earnings would have been had the nonamortization provisions of Statement No. 142 been applied in those years. Those reconciliations, including related per share amounts, are as follows:

	Years ended December 31		
	2002	*2001*	*2000*
Reported net earnings	$345.6	$267.0	$221.0
Add back: Goodwill amortization	–	11.3	11.1
Add back: Assembled workforce amortization	–	0.8	0.4
Adjusted net earnings	$345.6	$279.1	$232.5
Basic net earnings per share:			
Reported basic net earnings per share	$1.75	$1.36	$1.13
Goodwill amortization	–	$.06	$.06
Assembled workforce amortization	–	–	–
Adjusted basic net earnings per share	$1.75	$1.42	$1.19
Diluted net earnings per share:			
Reported diluted net earnings per share	$1.70	$1.32	$1.10
Goodwill amortization	–	$.06	$.06
Assembled workforce amortization	–	–	–
Adjusted diluted net earnings per share	$1.70	$1.37	$1.16

The changes in the net carrying amount of goodwill by segment for the year ended December 31, 2002 are as follows:

	Orthopaedic Implants	MedSurg Equipment	Other	Total
Balances as of January 1, 2002	$313.4	$102.3	$18.6	$434.3
Reclassification of assembled workforce intangible to goodwill	4.8	0.7	–	5.5
Reclassification of goodwill to other intangibles	–	(0.8)	–	(0.8)
Goodwill acquired	–	–	1.1	1.1
Reductions	(0.2)	–	–	(0.2)
Foreign currency translation effects	16.7	3.4	–	20.1
Balances as of December 31, 2002	$334.7	$105.6	$19.7	$460.0

Other intangibles at December 31, 2002 consist of the following:

	Gross Carrying Amount	Less Accumulated Amortization	Net Carrying Amount
Amortized intangible assets:			
Developed technology	$220.3	$48.5	$171.8
Customer relationships	146.6	15.9	130.7
Patents	156.1	22.9	133.2
Trademarks	29.2	3.0	26.2
Other	22.2	9.0	13.2
Total	$574.4	$99.3	$475.1

Amortization expense for other intangibles totaled $28.9 for the year ended December 31, 2002. The estimated amortization expense for each of the five succeeding years is as follows:

2003	$34.6
2004	$34.6
2005	$32.7
2006	$30.1
2007	$30.1

NOTE 6
RESTRUCTURING AND ACQUISITION-RELATED LIABILITIES

The Company recorded restructuring and acquisition-related pretax charges (credits) consisting of the following items:

	2002	*2001*	*2000*
Restructuring charges (credits):			
Severance and related costs	$21.0	($0.6)	$1.3
Reorganization of distribution channels	–	0.7	(2.1)
Discontinuance of product line	–	(0.4)	(0.4)
Other	–	–	1.4
Total restructuring charges (credits)	21.0	(0.3)	0.2
Acquisition-related charges (credits):			
Severance and related costs	–	0.9	–
Reorganization of distribution channels	–	–	(1.2)
Reductions	(3.8)	–	–
Total acquisition-related charges (credits)	(3.8)	0.9	(1.2)
Total restructuring and acquisition-related charges (credits)	$17.2	$0.6	($1.0)

The 2002 restructuring and acquisition-related items reflect a charge of $17.2 ($11.5 net of income taxes) in the third quarter of 2002. These items include a charge of $21.0 ($14.1 net of income taxes) for employment-related costs to close the Company's Rutherford, New Jersey manufacturing facility, partially offset by a credit of $3.8 ($2.6 net of income taxes) to reverse certain Howmedica restructuring and acquisition-related costs to reflect actual final payments required.

The $21.0 restructuring charge relates to the shutdown agreement reached between the Company and the employee bargaining unit to close the Howmedica Osteonics implant manufacturing facility in Rutherford, New Jersey which was ratified by the members of the I.U.E.-CWA Local 485 on August 23, 2002. Under the agreement, laid-off employees will receive significantly more benefits than they would have under the Collective Bargaining Agreement that was set to expire on August 31, 2002. In addition, at least 80 qualified employees from the Rutherford facility will be offered employment at the new Howmedica Osteonics facility in Mahwah, New Jersey. The charge covers employment-related severance costs for approximately 400 employees. The Company expects the Rutherford facility to be closed over the next 12 months with final severance payments to be made in 2004. As Howmedica Osteonics prepares to permanently cease manufacturing in Rutherford, it will transition production to its facilities in Mahwah, New Jersey as well as Cork and Limerick, Ireland.

The 2001 restructuring credits of $0.3 relate to various restructuring events in the fourth quarter of 2001. The $0.6 credit for severance and related costs reflects charges of $0.8 offset by credits of $1.4. The $0.8 charge covers severance costs for 10 employees in Europe. Planned workforce reductions were completed in the first quarter of 2002. The $1.4 credit relates to a reduction in the expected cost to complete headcount reductions associated with the 2000 and 1999 reorganizations of the Company's European and Japanese distribution operations. The $0.7 charge related to reorganization of distribution channels reflects the cost to terminate a distributor in Latin America. The cost of the termination is based on contractual terms. The $0.4 credit related to discontinuance of product line represents a reversal of remaining loss reserves established in Japan for discontinued ophthalmology inventories sold on a contingent basis in 1999.

The 2001 acquisition-related charges include $0.9 for severance and related costs associated with the reorganization of the Company's sales structure in Italy to accommodate the integration of the business acquired in the fourth quarter of 2001 from the Company's independent Italian distributor (see Note 4). The reorganization established a direct sales force in Italy that will distribute the Company's full product portfolio. The $0.9 charge covers severance costs for three employees in Italy and costs to cancel contracts with discontinued agents. The reorganization of the sales structure in Italy was completed in the first quarter of 2002.

The 2000 restructuring charges of $0.2 relate to various restructuring events in the fourth quarter of 2000. Severance and related costs of $1.3 reflect charges of $4.0 partially offset by a credit of $2.7. The $4.0 charge covers severance costs for 95 employees, primarily in Europe. The planned workforce reductions were completed in 2001, and the remaining amount of this reserve was reversed in 2001. The $2.7 credit relates to a reduction in the expected cost to complete the headcount reductions associated with the 1999 reorganization of the Company's Japanese distribution operations. The credit of $2.1 related to reorganization of distribution channels reflects a charge of $0.6 to terminate two small European distributors, offset by a credit of $2.7 to reverse reserves for a distributor reorganization that was charged to operations in 1996. The delay in the use of the 1996 reserves occurred because the distributor is located in a country where Howmedica had a direct sales operation. The purchase of the Howmedica assets in this country was delayed because of the lengthy regulatory approval process there and was completed in 2000. After evaluating its business in this country, the Company decided not to terminate the distributor and reversed the previously recorded reserve. The $0.4 credit related to discontinuance of product line represents a reversal of a portion of the loss reserves established in Japan for discontinued ophthalmology inventories sold on a contingent basis in 1999. The other charges of $1.4 represent asset write-offs, primarily for goodwill and inventory, and lease commitments associated with certain operations, principally in Europe, that were closed in the fourth quarter of 2000.

The acquisition-related credit of $1.2 in 2000 reflected a reduction in the expected cost to complete the conversion of the remaining Osteonics distributors in the United States and certain distributors in Europe and the Pacific region to direct sales in the form of branches or agents to accommodate the integration of the Howmedica sales force. These conversions provided the Company greater control over the distribution channels and facilitated the integration with the Howmedica organization. The cost of the conversions was based on contractual terms.

The following table provides a rollforward of remaining liabilities associated with business acquisition purchase liabilities and restructuring and acquisition-related charges recorded by the Company in 2002, 2001 and prior years:

	Distributor Conversions	Severance and Related Costs	Facility Closures and Contractual Obligations	Other
Balances at January 1, 2001	$7.0	$6.4	$6.7	$4.7
Additions (reductions) recognized as charges (credits) in the 2001 Consolidated Statement of Earnings	0.7	0.3	–	(0.4)
Payments	(2.3)	(3.4)	(5.2)	(0.3)
Reductions	–	(0.1)	(0.1)	–
Foreign currency translation effects	(0.1)	(0.5)	(0.1)	–
Balances at December 31, 2001	5.3	2.7	1.3	4.0
Additions (reductions) recognized as charges (credits) in the 2002 Consolidated Statement of Earnings	–	21.0	–	(3.8)
Additions from business acquisitions	–	3.1	0.5	–
Payments	(2.3)	(4.7)	(1.2)	(0.2)
Foreign currency translation effects	–	(0.2)	–	–
Balances at December 31, 2002	$3.0	$21.9	$0.6	$0.0

NOTE 7
BORROWINGS AND OTHER FINANCING ARRANGEMENTS

Long-term debt is as follows:

	December 31	
	2002	*2001*
United States dollar revolving loans	$447.0	$650.0
Multicurrency loans	39.9	67.2
Other	14.8	5.4
	501.7	722.6
Less current maturities	10.7	1.7
	$491.0	$720.9

In December 2001, the Company established $1,000.0 in Unsecured Credit Facilities. These Facilities replaced the $1,650.0 Senior Secured Credit Facilities that were established in 1998 in conjunction with the acquisition of Howmedica. A total of $730.5 was initially drawn under the new Credit Facilities, of which $642.7 prepaid the debt outstanding under the 1998 Facilities and $87.8 was used to terminate the Company's synthetic lease and purchase its Mahwah, New Jersey manufacturing and distribution facility.

The Unsecured Credit Facilities include a $250.0 364-day revolving credit agreement and a $750.0 five-year, nonamortizing, revolving credit agreement. The $250.0 364-day revolving credit agreement bears interest at a base rate, as defined, plus an applicable margin ranging from 0.245% to 0.800%, depending on the Company's debt rating. The $750.0 five-year, nonamortizing, revolving credit agreement has a $250.0 multicurrency sublimit, under which yen and euro can be borrowed. The five-year facility also has a $50.0 swing line sublimit and a $100.0 letter of credit sublimit. The five-year facility bears interest at a base rate, as defined, plus an applicable margin ranging from 0.235% to 0.775%, depending on the Company's

debt rating. The Unsecured Credit Facilities require a commitment fee ranging from 0.055% to 0.225% on the aggregate commitment of the facilities, depending on the Company's debt rating. In addition, a utilization fee of 0.125% is required when the sum of the outstanding amounts exceeds 50% of the aggregate commitments. During 2002, the weighted average interest rate for all borrowings under the Unsecured Credit Facilities, after considering the effects of the Company's interest rate swaps, was 5.33%. The Facilities require the Company to comply with certain financial and other covenants.

At December 31, 2002, the Company had borrowed yen 4,820.5 under the multicurrency sublimit available under the five-year revolving credit agreement. The yen borrowing acts as a hedge of a portion of the Company's net investment in Japan. As a result, adjustments made to the loan balance to reflect applicable currency exchange rates at December 31 are included within accumulated other comprehensive gain (loss) in stockholders' equity.

The $1,650.0 Senior Secured Credit Facilities that were prepaid in December 2001 consisted of $1,150.0 in term loans, a six-year $250.0 revolving credit facility and a six-year $250.0 reducing multicurrency facility. The Senior Secured Credit Facilities had a weighted average interest rate for all borrowings, after considering the effects of the Company's interest rate swaps, of 7.05% during 2001.

The prepayment of the remaining amounts outstanding under the Senior Secured Credit Facilities in December 2001 resulted in the write-off of related unamortized deferred loan costs of $7.1, which was reflected as an extraordinary loss of $4.8 (net of income taxes of $2.3; $.02 per basic and diluted share) in the Consolidated Statements of Earnings.

The Company has fixed the base rate on a $250.0 notional amount of the variable-rate borrowings at an average rate of 5.58% using interest rate swaps (see Note 2).

Maturities of debt for the four years succeeding 2003 are: 2004 - $0.2; 2005 - $0.2; 2006 - $487.1; and 2007 - $0.2.

The carrying amounts of the Company's long-term debt approximate their fair values, based on the quoted interest rates for similar types and amounts of borrowing agreements.

Interest paid on debt was $37.1 in 2002, $66.9 in 2001 and $94.3 in 2000 and approximates interest expense.

NOTE 8
CAPITAL STOCK

The Company has key employee and director stock option plans under which options are granted at a price not less than fair market value at the date of grant. The options are granted for periods of up to 10 years and become exercisable in varying installments. A summary of stock option activity follows:

	Shares	Weighted-Average Exercise Price
Options outstanding at January 1, 2000	9.7	$15.18
Granted	2.8	32.45
Canceled	(0.2)	23.41
Exercised	(1.1)	7.42
Options outstanding at December 31, 2000	11.2	20.19
Granted	2.0	46.86
Canceled	(0.2)	26.78
Exercised	(0.8)	13.06
Options outstanding at December 31, 2001	12.2	24.87
Granted	2.0	52.90
Canceled	(0.3)	36.00
Exercised	(1.5)	13.19
Options outstanding at December 31, 2002	12.4	$30.43
Price range $5.59 - $10.00	0.6	$6.10
Price range $10.01 - $20.00	3.3	14.68
Price range $20.01 - $30.00	2.3	24.25
Price range $30.01 - $40.00	2.4	32.41
Price range $40.01 - $50.00	1.8	46.58
Price range $50.01 - $57.05	2.0	52.89
Options outstanding at December 31, 2002	12.4	$30.43

Shares reserved for future grants were 9.5 and 11.2 at December 31, 2002 and 2001, respectively.

Exercise prices for options outstanding as of December 31, 2002 ranged from $5.59 to $57.05. A summary of shares exercisable follows:

	Shares	Weighted-Average Exercise Price
Price range $5.59 - $10.00	0.6	$6.10
Price range $10.01 - $20.00	3.0	14.41
Price range $20.01 - $30.00	1.3	24.24
Price range $30.01 - $40.00	0.9	32.41
Price range $40.01 - $53.39	0.4	46.82
Shares exercisable at December 31, 2002	6.2	$20.44

On April 19, 2000, the Company's stockholders approved an amendment to the Company's Restated Articles of Incorporation to increase its authorized shares of common stock to 500.0 from 150.0.

On April 19, 2000, the Company's Board of Directors approved a two-for-one stock split effective May 12, 2000 for stockholders of record on May 1, 2000.

All share and per share data have been adjusted to reflect the increase in authorized shares and the stock split as though they had occurred at the beginning of the periods presented.

The Company has 0.5 authorized shares of $1 par value preferred stock, none of which are outstanding.

NOTE 9
EARNINGS PER SHARE

The following table sets forth the computation of basic and diluted earnings per share:

	2002	*2001*	*2000*
Earnings before extraordinary item	$345.6	$271.8	$221.0
Extraordinary loss, net of income taxes	–	(4.8)	–
Net earnings	$345.6	$267.0	$221.0
Weighted-average shares outstanding for basic earnings per share	197.5	196.3	195.1
Effect of dilutive employee stock options	6.3	6.7	6.0
Adjusted weighted-average shares outstanding for diluted earnings per share	203.8	203.0	201.1
Basic earnings per share of common stock:			
Before extraordinary item	$1.75	$1.38	$1.13
Extraordinary loss	–	($.02)	–
Net earnings	$1.75	$1.36	$1.13
Diluted earnings per share of common stock:			
Before extraordinary item	$1.70	$1.34	$1.10
Extraordinary loss	–	($.02)	–
Net earnings	$1.70	$1.32	$1.10

NOTE 10
RETIREMENT PLANS

Certain of the Company's subsidiaries have defined benefit plans covering some or all of their employees. All of the defined benefit plans have benefit obligations in excess of plan assets. A summary of the information related to all of the Company's defined benefit plans is as follows:

	December 31	
	2002	*2001*
Change in benefit obligations:		
Benefit obligations at beginning of year	$68.5	$71.3
Service cost	4.5	3.9
Interest cost	4.2	4.1
Foreign exchange impact	6.0	(2.2)
Employee contributions	0.3	0.4
Plan amendments	0.7	0.4
Actuarial and curtailment losses	6.6	2.0
Plan termination	–	(8.1)
Benefits paid	(3.9)	(3.3)
Benefit obligations at end of year	86.9	68.5
Change in plan assets:		
Fair value of plan assets at beginning of year	48.0	59.8
Actual return	(4.5)	(1.3)
Employer contributions	3.3	3.8
Employee contributions	0.3	0.4
Foreign exchange impact	3.2	(1.5)
Plan termination	–	(9.9)
Benefits paid	(3.6)	(3.3)
Fair value of plan assets at end of year	46.7	48.0
Amount underfunded	(40.2)	(20.5)
Unrecognized net actuarial loss (gain)	17.2	(1.6)
Unrecognized transition amount	0.6	0.7
Unrecognized prior service cost	2.8	2.1
Net amount recognized in Consolidated Balance Sheets	($19.6)	($19.3)
Weighted-average assumptions as of December 31:		
Discount rate	5.5%	6.1%
Expected return on plan assets	5.2%	6.6%
Rate of compensation increase	3.1%	3.3%

The components of the amounts recognized in the Consolidated Balance Sheets are as follows:

	December 31	
	2002	*2001*
Prepaid benefit cost	$0.8	$0.5
Accrued benefit liability	(20.4)	(19.8)
Additional minimum liability	(12.6)	–
Intangible asset	2.8	–
Accumulated other comprehensive loss	9.8	–
Net amount recognized	($19.6)	($19.3)

Pension plans with an accumulated benefit obligation in excess of plan assets had projected benefit obligations, accumulated benefit obligations and fair value of plan assets of $63.6, $59.8 and $29.9, respectively, as of December 31, 2002.

The components of net periodic benefit cost for the plans are as follows:

	2002	*2001*	*2000*
Service cost	$4.5	$3.9	$3.8
Interest cost	4.2	4.1	3.9
Expected return on plan assets	(3.4)	(3.8)	(3.9)
Amortization of transition amounts and prior service cost	0.2	0.3	0.3
Recognized actuarial gain	–	(0.2)	(0.2)
Plan termination loss	–	0.5	–
Net periodic benefit cost	$5.5	$4.8	$3.9

A subsidiary of the Company terminated its defined benefit plan in 2001 and transferred the plan assets and related benefit obligations to a defined contribution retirement plan. The loss on plan termination was $0.5.

Retirement plan expense under the Company's profit sharing and defined contribution retirement plans totaled $45.2 in 2002, $36.5 in 2001 and $31.9 in 2000. A portion of the Company's retirement plan expenses was funded with Stryker common stock totaling $4.1 in 2002, $3.4 in 2001 and $3.1 in 2000. The use of Stryker common stock represents a noncash investing activity that is not reflected in the Consolidated Statements of Cash Flows. The amount of Stryker common stock held by the Company's defined contribution retirement plans totaled $51.5 (0.8 shares) and $42.6 (0.7 shares) as of December 31, 2002 and 2001, respectively. The value of Stryker common stock as a percentage of total defined contribution retirement plan assets was 20.2% as of December 31, 2002 and 17.9% as of December 31, 2001.

NOTE 11
INCOME TAXES

Earnings before income taxes and extraordinary item consist of the following:

	2002	*2001*	*2000*
United States operations	$246.1	$241.2	$197.4
Foreign operations	260.6	164.5	137.5
	$506.7	$405.7	$334.9

In 2002, earnings from the Company's Puerto Rico-based manufacturing operations are reported as foreign operations due to a change in legal status. Prior to 2002, these earnings were reported as United States operations under an Internal Revenue Code Section 936 election.

The components of the provision for income taxes follow:

	2002	*2001*	*2000*
Current income tax expense:			
Federal	$80.0	$51.4	$44.8
State, including Puerto Rico in 2001 and 2000	6.9	14.2	10.1
Foreign	76.0	39.2	30.3
	162.9	104.8	85.2
Deferred income tax expense (credit)	(1.8)	29.1	28.7
	$161.1	$133.9	$113.9

A reconciliation of the United States statutory income tax rate to the Company's effective income tax rate follows:

	2002	*2001*	*2000*
United States statutory income tax rate	35.0%	35.0%	35.0%
Add (deduct):			
State taxes, less effect of federal deduction	0.8	1.5	1.7
Tax benefit relating to operations in Ireland and Puerto Rico	(7.8)	(7.1)	(6.9)
Tax benefit relating to United States export sales	(1.4)	(0.9)	(2.2)
Nondeductible (deductible) permanent differences	1.2	(1.3)	3.7
Tax benefit relating to foreign tax credit	(0.5)	(0.1)	(2.2)
Foreign income taxes at rates different from the United States statutory rate	3.6	6.7	7.1
Other	0.9	(0.8)	(2.2)
	31.8%	33.0%	34.0%

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. The tax effect of significant temporary differences, which comprise the Company's deferred tax assets and liabilities, is as follows:

	December 31	
	2002	*2001*
Deferred tax assets:		
Inventories	$137.9	$84.6
Accounts receivable and other assets	16.1	7.9
Other accrued expenses	49.1	33.5
Depreciation and amortization	41.8	33.3
State taxes	7.8	7.5
Net operating loss carryforwards	22.4	34.4
Other	14.2	30.7
Total deferred tax assets	289.3	231.9
Deferred tax liabilities:		
Depreciation and amortization	(55.0)	(33.7)
Other accrued expenses	(7.3)	(5.0)
Interest rate swaps	(1.1)	(7.6)
Other	(11.8)	(18.4)
Total deferred tax liabilities	(75.2)	(64.7)
Total net deferred tax assets	$214.1	$167.2

Net operating loss carryforwards totaling approximately $64.9 at December 31, 2002 are available to reduce future taxable earnings of certain foreign subsidiaries. A significant portion of these carryforwards may be carried forward indefinitely.

Deferred tax assets and liabilities are included in the Consolidated Balance Sheets as follows:

	December 31	
	2002	*2001*
Current assets—Deferred income taxes	$227.5	$171.5
Noncurrent assets—Deferred income taxes	61.8	60.4
Current liabilities—Accrued expenses and other liabilities	(28.7)	(12.0)
Noncurrent liabilities—Other liabilities	(46.5)	(52.7)
Total net deferred tax assets	$214.1	$167.2

No provision has been made for United States federal and state income taxes or foreign taxes that may result from future remittances of the undistributed earnings ($660.7 at December 31, 2002) of foreign subsidiaries because it is expected that such earnings will be reinvested overseas indefinitely. Determination of the amount of any unrecognized deferred income tax liability on these unremitted earnings is not practicable.

Total income taxes paid, net of refunds received, were $112.1 in 2002, $63.0 in 2001 and $75.3 in 2000.

NOTE 12
SEGMENT AND GEOGRAPHIC DATA

The Company segregates its operations into two reportable business segments: Orthopaedic Implants and MedSurg Equipment. The Orthopaedic Implants segment sells orthopaedic reconstructive (hip, knee and shoulder), trauma and spinal implants, bone cement and OP-1. The MedSurg Equipment segment sells powered surgical instruments, endoscopic systems,

medical video imaging equipment, hospital beds and stretchers, craniomaxillofacial implants and image-guided surgical systems. Other includes Physical Therapy Services and corporate administration, interest expense and interest income.

The Company's reportable segments are business units that offer different products and services and are managed separately because each business requires different manufacturing, technology and marketing strategies.

The accounting policies of the segments are the same as those described in the summary of significant accounting policies. The Company evaluates performance based on net earnings of each segment. Identifiable assets are those assets used exclusively in the operations of each business segment or are allocated when used jointly. Corporate assets are principally cash and cash equivalents, investments and property, plant and equipment.

Sales and other financial information by business segment follows:

	Orthopaedic Implants	MedSurg Equipment	Other	Total
Year ended December 31, 2002				
Net sales	$1,704.8	$1,105.3	$201.5	$3,011.6
Interest income	–	–	2.4	2.4
Interest expense	–	–	40.3	40.3
Depreciation and amortization expense	146.4	32.8	6.9	186.1
Restructuring and acquisition-related charges (credits)	21.0	–	(3.8)	17.2
Income taxes (credit)	118.6	56.4	(13.9)	161.1
Segment net earnings (loss)	234.8	135.4	(24.6)	345.6
Total assets	2,062.3	625.3	127.9	2,815.5
Capital expenditures	90.7	29.4	18.9	139.0
Year ended December 31, 2001				
Net sales	1,447.2	974.2	180.9	2,602.3
Interest income	–	–	2.2	2.2
Interest expense	–	–	67.9	67.9
Depreciation and amortization expense	129.6	34.6	7.8	172.0
Restructuring and acquisition-related charges (credits)	0.8	(0.2)	–	0.6
Income taxes (credit)	111.1	54.5	(31.7)	133.9
Segment earnings (loss) before extraordinary item	197.7	115.5	(41.4)	271.8
Extraordinary loss, net of income taxes	–	–	(4.8)	(4.8)
Segment net earnings (loss)	197.7	115.5	(46.2)	267.0
Total assets	1,737.6	574.6	111.4	2,423.6
Capital expenditures	133.5	21.6	6.8	161.9
Year ended December 31, 2000				
Net sales	1,315.6	826.5	147.3	2,289.4
Interest income	–	–	4.1	4.1
Interest expense	–	–	96.6	96.6
Depreciation and amortization expense	132.8	29.6	6.2	168.6
Restructuring and acquisition-related charges (credits)	(1.8)	0.5	0.3	(1.0)
Income taxes (credit)	112.7	50.5	(49.3)	113.9
Segment net earnings (loss)	174.1	103.4	(56.5)	221.0
Total assets	1,739.1	588.2	103.5	2,430.8
Capital expenditures	56.5	19.1	5.1	80.7

The Company's principal areas of operation outside of the United States are Europe and Japan. The Company also has operations in the Pacific, Canada, Latin America and the Middle East. Geographic information follows:

	Net Sales	Long-Lived Assets
Year ended December 31, 2002		
United States	$1,973.7	$930.2
Europe	497.1	531.2
Japan	275.3	102.4
Other foreign countries	265.5	38.6
	$3,011.6	$1,602.4
Year ended December 31, 2001		
United States	$1,688.4	$780.7
Europe	414.5	455.6
Japan	266.5	94.1
Other foreign countries	232.9	39.7
	$2,602.3	$1,370.1
Year ended December 31, 2000		
United States	$1,408.2	$715.4
Europe	380.5	472.9
Japan	280.1	119.3
Other foreign countries	220.6	42.2
	$2,289.4	$1,349.8

NOTE 13
LEASES

The Company leases various manufacturing and office facilities and equipment under operating leases. Future minimum lease commitments under these leases are as follows:

2003	$40.0
2004	31.5
2005	22.7
2006	16.8
2007	13.4
Thereafter	45.3
	$169.7

Rent expense totaled $61.3 in 2002, $51.6 in 2001 and $42.2 in 2000.

NOTE 14
CONTINGENCIES

The Company is involved in various proceedings, legal actions and claims arising in the normal course of business, including proceedings related to product, labor and other matters. Such matters are subject to many uncertainties, and outcomes are not predictable with assurance. The Company records amounts for losses that are deemed to be probable and subject to reasonable estimate. However, the Company does not anticipate material losses as a result of these proceedings beyond amounts already provided in the accompanying financial statements.

Pursuant to certain of the Company's credit and lease agreements, the Company has provided financial guarantees to third parties in the form of indemnification provisions. These provisions indemnify the third parties for costs, including but not limited to adverse judgments in lawsuits and the imposition of additional taxes due to either a change in the tax law or an adverse interpretation of the tax law. The term of the guarantee is equal to the term of the related credit or lease agreement. The Company is not able to calculate the maximum potential amount of future payments it could be required to make under these guarantees, as the potential payment is dependent on the occurrence of future unknown events (e.g., changes in United States or foreign tax laws).

SUMMARY OF QUARTERLY DATA (UNAUDITED) Stryker Corporation and Subsidiaries

(in millions, except per share data)

	2002 Quarter Ended				2001 Quarter Ended			
	March 31	June 30	Sept. 30	Dec. 31	March 31	June 30	Sept. 30	Dec. 31
Net sales	$702.9	$733.9	$745.6	$829.2	$634.2	$639.0	$619.3	$709.8
Gross profit	448.0	466.8	465.7	519.9	401.9	401.7	390.5	444.4
Earnings before extraordinary item and income taxes	121.0	128.2	108.2	149.3	95.7	98.1	90.4	121.5
Earnings before extraordinary item	81.1	85.9	72.5	106.1[a]	64.1	65.7	60.6	81.4
Extraordinary loss, net of income taxes	–	–	–	–	–	–	–	(4.8)
Net earnings	81.1	85.9	72.5	106.1[a]	64.1	65.7	60.6	76.6
Net earnings per share of common stock:								
Basic	.41	.44	.37	.54	.33	.33	.31	.41[b]
Diluted	.40	.42	.36	.52	.32	.32	.30	.40[b]
Market price of common stock:								
High	63.00	60.65	60.50	67.47	57.00	59.95	63.20	59.40
Low	53.25	50.90	43.85	56.76	43.30	49.04	44.78	51.19

The price quotations reported above were supplied by the New York Stock Exchange.

(a) In the fourth quarter of 2002, the Company reduced the effective tax rate for the year to 31.8% from 33.0%, thereby decreasing income tax expense by $6.1.
(b) Excludes net extraordinary loss per share of $.02 basic and $.02 diluted.

REPORT OF INDEPENDENT AUDITORS

The Board of Directors and Stockholders of Stryker Corporation:

We have audited the accompanying consolidated balance sheets of Stryker Corporation and subsidiaries as of December 31, 2002 and 2001, and the related consolidated statements of earnings, stockholders' equity and cash flows for each of the three years in the period ended December 31, 2002. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Stryker Corporation and subsidiaries at December 31, 2002 and 2001, and the consolidated results of their operations and their cash flows for each of the three years in the period ended December 31, 2002, in conformity with accounting principles generally accepted in the United States.

As discussed in Note 5 to the financial statements, in 2002 the Company changed its method of accounting for goodwill and, as discussed in Note 1, in 2001 the Company changed its method of accounting for derivative financial instruments.

Ernst & Young LLP

Grand Rapids, Michigan
January 28, 2003

BOARD OF DIRECTORS

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Chairman, President and Chief Executive Officer,
Stryker Corporation

Howard E. Cox, Jr. † ‡
General Partner, Greylock

*Donald M. Engelman, Ph.D.** ‡
Eugene Higgins Professor of Molecular Biophysics and Biochemistry, Yale University, and Chair of the Science and Technology Steering Committee for the Brookhaven National Laboratory

*Jerome H. Grossman, M.D.** ‡
Director of the Harvard/Kennedy School Health Care Delivery Policy Program at Harvard University and Chairman and Chief Executive Officer, Lion Gate Management Corporation

*John S. Lillard** ‡
Chairman, Wintrust Financial Corporation

*William U. Parfet** † ‡
Chairman and Chief Executive Officer, MPI Research, Inc.

Ronda E. Stryker † ‡
Granddaughter of the founder of the Company and daughter of the former President of the Company, Vice Chairman and Director of Greenleaf Trust, Vice Chairman and Trustee of Kalamazoo College, Vice President and Trustee of the Kalamazoo Institute of Arts and Trustee of the Kalamazoo Foundation and Spelman College

* Audit Committee
† Compensation Committee
‡ Governance and Nominating Committee

CORPORATE OFFICERS

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Chairman, President and Chief Executive Officer

J. Patrick Anderson
Vice President of Business Development and Assistant to the Chairman

Dean H. Bergy
Vice President, Chief Financial Officer and Secretary

Curtis E. Hall, Esq.
General Counsel

Christopher F. Homrich
Vice President and Treasurer

Stephen Si Johnson
Vice President; Group President, Stryker MedSurg

James E. Kemler
Vice President; Group President, Stryker Biotech, Spine and Trauma

James R. Lawson
Vice President; Group President, Stryker International

Edward B. Lipes
Vice President; Group President, Stryker Howmedica Osteonics

Eric Lum
Vice President, Tax

Michael R. Mainelli, Jr.
Vice President; President, Stryker Spine

James B. Praeger
Controller

Michael W. Rude
Vice President of Human Resources

David J. Simpson
Executive Vice President

Thomas R. Winkel
Vice President of Administration

Jeffrey R. Winter
Vice President, Internal Audit

STRYKER HOWMEDICA OSTEONICS

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Jeffrey B. Paulsen – Senior Vice President, Chief Operating Officer

Bradford J. Williams – Senior Vice President, Reconstructive Business

STRYKER MEDSURG

Stephen Si Johnson – Group President

Stryker Canada
Robert E. Bentley – Vice President, General Manager

Stryker Endoscopy
William R. Enquist – President

Stryker Instruments
Curt R. Hartman – Vice President, General Manager

Stryker Latin America
Thomas A. Hedges – General Manager

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Eric L. Teutsch – Vice President, General Manager

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Jason T. Blackwood – President

STRYKER BIOTECH, SPINE AND TRAUMA

James E. Kemler – Group President

Stryker Biotech
Timothy J. Scannell – Vice President, General Manager

Stryker Spine
Michael R. Mainelli, Jr. – President

Stryker Trauma
Vivian Masson – President

STRYKER INTERNATIONAL

James R. Lawson – Group President

Stryker Europe
Luciano Cattani – President

Stryker Japan
Yoshiaki Nakazawa – President

Stryker Pacific
Andrew Fox-Smith – Vice President, General Manager

General Counsel
Winston & Strawn, New York, New York

Auditors
Ernst & Young LLP, Grand Rapids, Michigan

Transfer Agent and Registrar
National City Bank, Cleveland, Ohio

Shareholders needing information regarding their certificates or dividends should contact:

National City Bank
Corporate Trust Operations
P.O. Box 92301
Cleveland, Ohio 44193-0900
(1-800-622-6757)
shareholder.inquiries@nationalcity.com

Investor Contact
Dean H. Bergy, Vice President, Chief Financial Officer and Secretary

Annual Meeting
The Annual Meeting of Stockholders of Stryker Corporation will be held at the Radisson Plaza Hotel at The Kalamazoo Center, Kalamazoo, Michigan, on Tuesday, April 22, 2003, at 2:00 p.m.

Form 10-K
The Company files Form 10-K with the Securities and Exchange Commission. Shareholders wishing a copy of the 2002 report may obtain it free of charge at www.strykercorp.com or request it by writing to:

Secretary
Stryker Corporation
P.O. Box 4085
Kalamazoo, MI 49003-4085

Trademarks
Stryker Corporation or its subsidiaries own the registered trademarks: Accolade, Big Wheel, Chaperone, Crossfire, Cub, EIUS, Endosuite, EON, Exeter, Go Bed, Howmedica, Leibinger, OP-1, Osteonics, PainPump, Purefix, Ray Threaded Fusion Cage, Scorpio, Secure, Stryker, TMZF, Trident, Trio, Xia and Zoom; and the trademarks: DEKOMPRESSOR, Gamma, Reflex, ScorpioFlex, SDC Pro 2, Secur-Fit, SMARTLock, SuperFlex and T2. The service mark Physiotherapy Associates is also used in this report.

Stock Listing
The Company's common stock is traded on the New York Stock Exchange under the symbol SYK.

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