

Stock Discussion Group (SDG)

February 26 2005

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SDG Meeting Purpose



- Discuss investing topics
- Expand knowledge
- Share experiences
- Q&A opportunity
- Learn and Earn More

SDG Agenda

- **Information**
- **Watch Lists**
- **Quality of Stryker**
- **SSG Study of Stryker**

Information

- Sign in sheets – Need email addresses
- Next SDG Meeting 3/12
- CNCC Fair 4/2 – Flyer Available
- Portfolio results now on CNCC Web site
 - <http://www.bivio.com/cncc/accounting/reports/>
- Announcements of future events now on handout
- Survey handout – How can we improve?
 - Include Email Address
 - Desired Future Topics

SDG Portfolio

Data as of 2/18/05

	IRR	Portfolio Value
Central North Carolina Chapter NAIC	<u>14.2%</u>	<u>20,241.28</u>
Vanguard Total Stock Market Index Fund (VTSMX)	13.6%	20,147.44
Vanguard 500 Index Fund (VFINX)	12.5%	19,974.09

SDG Portfolio – 2/18/05

	Shares Held	Cost Basis per Share	Total Cost Basis	Price per Share	Market Value	Unrealized Gain/(Loss)	Percent of Total
Affiliated Computer Services Inc (ACS)	40.0000	49.8950	1,995.80	52.8500	2,114.00	118.20	10.5%
Bed, Bath & Beyond Inc (BBBY)	55.0000	36.3373	1,998.55	37.8900	2,083.95	85.40	10.3%
Cardinal Health Inc (CAH)	30.0000	68.8133	2,004.40	58.3500	1,750.50	(253.90)	8.7%
Fiserv Inc (FISV)	53.0000	37.8421	2,005.63	37.8200	2,004.46	(1.17)	9.9%
Johnson & Johnson (JNJ)	38.0000	51.9542	1,974.26	65.4300	2,486.34	512.08	12.3%
L-3 Communications Holdings Inc (LLL)	44.0000	45.9591	2,022.20	72.4600	3,188.24	1,166.04	15.8%
Medtronic Inc (MDT)	42.0000	48.1687	2,023.00	53.0000	2,226.00	203.00	11.0%
Pfizer Inc (PFE)	79.0000	25.3386	2,001.75	26.8000	2,117.20	115.45	10.5%
Williams-Sonoma Inc (WSM)	64.0000	30.8494	1,974.36	34.3700	2,199.68	225.32	10.9%
			<u>17,999.95</u>		<u>20,170.37</u>	<u>2,170.42</u>	<u>99.8%</u>

■ Attendee Stock Favorites

- Good Company
- Close to Providing Good Value
- Not Previously Studied
- Few words why to study

Watch List

- What is it?
- Why have one?
- How to implement?

What is a Watch List ?

- List of identified good companies that are currently priced too high to provide a reasonable return
 - Good Quality Growth Company
 - Price that would provide good value

Why Have A Watch List ?

- Stock prices will fluctuate
 - 50% change within a year is common
- When you perform your SSG may not be the best time to buy
- EPS Growth is a major contributor to return
- PE Expansion can make an average investment superior

Why Have A Watch List ?(cont)

Example – Stock A with EPS of \$1.00 and expected to grow at 10% per year. Impact of buying at PE of 20 or 16

Price PE	Cost 100Sh	EPS 5 Yrs	PE 5 Yrs	Value	Ann % Gain
20	2000	1.61	20	3221	10%
16	1600	1.61	20	3221	15+%

How to Implement ?

- Piece of paper
- Spreadsheet
- On-line Watch List
 - MSN, Yahoo, Quicken, etc
- On-line reminder
 - Yahoo
 - Sends email when stock price falls below your price target
 - <http://alerts.yahoo.com/>
- ALWAYS update SSG before buying

- For More on Watch Lists

- See Brian Lewis's info at:

- http://www.nwlink.com/~brianle/Brian_FA_Q.htm#Maintain_Watch_List

- Questions?

Is Stryker A High Quality Company?

- We will apply the January SDG discussion on “Identifying Quality Growth Companies” to determine

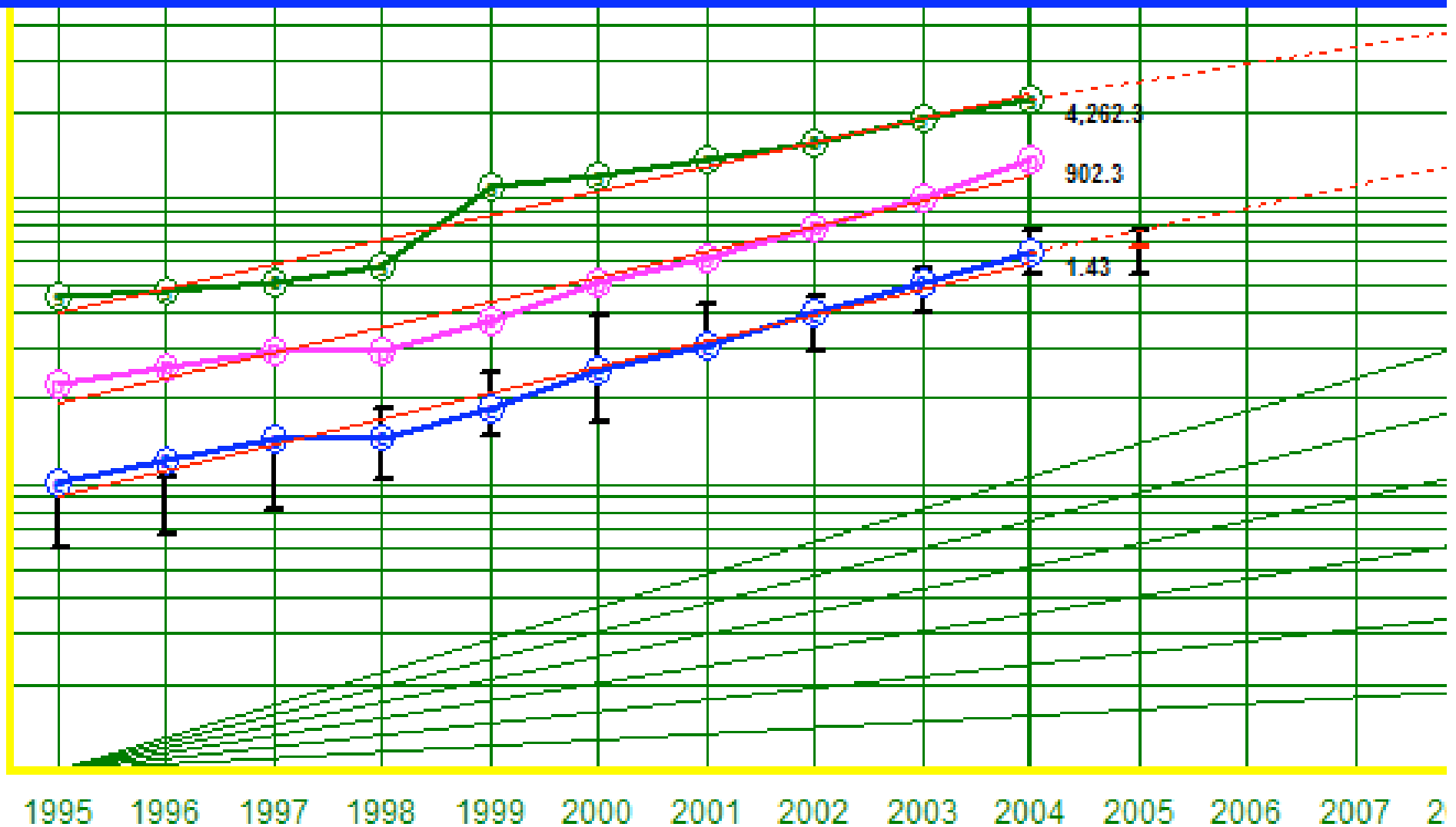
Ralph Seger Saying

The quality of a security is too often overlooked by investors; good-quality stocks frequently possess characteristics that are lacking in lesser-quality stocks. Low-quality stocks are liable to present you with an unexpected blown head gasket. In the final analysis, it is rare that a good quality stock gets so overvalued it should be sold.

Good Company SSG Criteria

1. Past & Projected Sales Growth is consistent and acceptable and an Industry Leader
2. Past & Projected EPS Growth is consistent and acceptable and an Industry Leader
3. Trend in % pre-tax profit to sales is steady or up and an industry leader
4. Trend in ROE % is steady or up and an industry leader

Stryker Visual Analysis

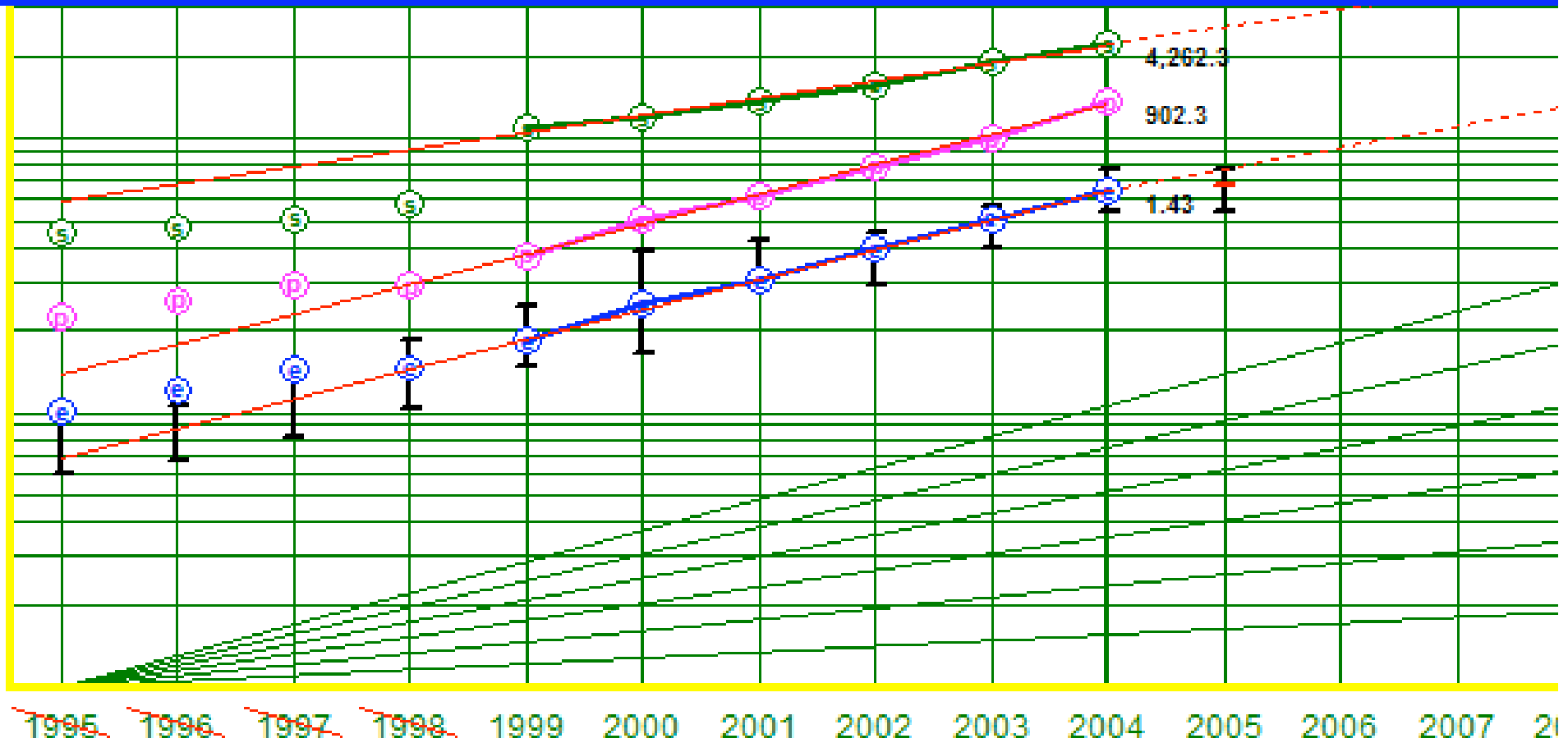


Hist. Sales Growth: 21.6



Hist. EPS Growth: 23.0

SYK with 95-98 OL's



Hist. Sales Growth: 15.5

Hist. EPS Growth: 28.3

Stryker Historical Growth

Number Years	% Sales Growth	% EPS Growth
9	21.6	23.0
8	22.8	24.1
7	23.1	25.7
6	21.3	28.3
5	15.5	28.3
4	17.1	27.5
3	18.1	28.7
2	19.0	27.8
1	17.6	27.1
R ²	0.95	0.98

Comparison of Growth Rates

SYK

BMET

ZMH

Number Years	% Sales Growth	% EPS Growth
9	21.6	23.0
8	22.8	24.1
7	23.1	25.7
6	21.3	28.3
5	15.5	28.3
4	17.1	27.5
3	18.1	28.7
2	19.0	27.8
1	17.6	27.1
R ²	0.95	0.98

Number Years	% Sales Growth	% EPS Growth
9	15.2	16.9
8	15.3	16.8
7	15.9	16.9
6	16.2	16.7
5	15.9	16.4
4	15.3	16.5
3	16.2	16.9
2	16.4	17.7
1	16.2	16.7
R ²	1.00	1.00

Number Years	% Sales Growth	% EPS Growth
4	18.4	20.7
3	21.6	20.7
2	27.0	27.0
1	38.5	26.7
R ²	0.94	0.95

Growth Rates

Stryker 2004 Sales = \$4.3B = Mid Size Company

SYK	Crit	Hist	VL Est	OPS	Zacks
Rev	≥ 9	15.5 / 21.6	11.6 / 13.4		
EPS	≥ 10	28.3	19.6	20.0	20.0

Sustainable Growth Rate = 28.5%

Company 2005 Guidance 1/26/05

Sales – Mid Double Digit - \$4.9B

Earnings - $>22\%$ to 1.74B

Impact of Expensing Stock Options - \$.06 to \$.08

Stryker Section 2

2 EVALUATING MANAGEMENT

Company STRYKER CORP (SYK)

02/10/05

	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	LAST 5 YEAR AVG.	TREND	
												UP	DOWN
A % Pre-tax Profit on Sales (Net Before Taxes + Sales)	16.9	18.6	19.8	17.5	11.7	14.6	15.6	17.4	18.2	21.2	17.4	UP	
B % Earned on Equity (EIS + Book Value)	19.2	19.7	20.1	18.5	23.5	25.2	25.0	23.1	20.9	22.2	23.3		DOWN
C % Debt to Equity (LT Debt + Bk Val + Strs)	21.4	17.0	0.7	221.3	175.8	102.4	68.3	32.8	0.9	0.0	40.9		DOWN

PTPM/ROE Comparison

		1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	LAST 5 YEAR AVG.	TREND	
													UP	DOWN
SYK	A % Pre-tax Profit on Sales (Net Before Taxes + Sales)	16.9	18.6	19.8	17.5	11.7	14.6	15.6	17.4	18.2	21.2	17.4	UP	
	B % Earned on Equity (E/S + Book Value)	19.2	19.7	20.1	18.5	23.5	25.2	25.0	23.1	20.9	22.2	23.3		DOWN
BME	A % Pre-tax Profit on Sales (Net Before Taxes + Sales)	27.6	28.0	29.1	31.3	31.9	31.8	32.7	32.3	32.1	31.4	32.0		DOWN
	B % Earned on Equity (E/S + Book Value)	17.9	17.8	18.9	18.6	19.2	19.3	18.6	20.4	21.6	22.1	20.4	UP	
ZMH	A % Pre-tax Profit on Sales (Net Before Taxes + Sales)						24.6	27.4	26.6	28.3	27.8	26.9	UP	
	B % Earned on Equity (E/S + Book Value)								253.7	69.8	12.8	112.1		DOWN

Morningstar Industry Comparison

Stock	Mkt Cap \$Mil	Sales \$Mil	Morningstar Stock Grades		
			Growth	Profit-ability	Financial Health
Stryker	20,371.0	4,108	B+	A	A+
Industry Average	1,679	468	C+	C+	B-
<u>Medtronic</u>	63,035	9,605	B	A+	A
<u>Boston Scientific</u>	27,868	4,963	A	A-	B
<u>Guidant</u>	23,198	3,792	B-	A	A+
<u>Baxter International</u>	21,194	9,451	B-	A-	C
<u>Zimmer Holdings</u>	20,402	2,881	A	A	A
<u>Becton, Dickinson and Co</u>	15,043	4,935	C+	A	A
<u>St. Jude Medical</u>	14,234	2,202	B+	A	A+
<u>Biomet</u>	11,037	1,683	B	A+	A
<u>Luxottica Group ADR</u>	9,994	3,164	---	---	---
<u>Smith & Nephew ADR</u>	9,864	2,196	---	---	---

Section 2

SYK	Crit	5 Yr Avg	2004	Trend
PTPM (2A)	Level / Up	17.4	21.4	Up
ROE (2B)	Level / Up	23.3	22.2	Down ?

Debt 2000 = \$876M, Debt 2004 = 0

Debt/Equity 2000 = 102.4

Debt/Equity 2004 = 0

Stryker Management

- **Management Change**

- John Brown CEO since 1977
- Under Brown SYK had 22% EPS growth last 27 years
- Steve McMillan replaces Brown in 2005
- Impact of new CEO?

- **CEO Compensation**

- 2003 Brown = \$2.1M + Options for 40000 shares
- 2005 McMillan Salary \$550K plus Potential Bonus of \$500K plus stock options

Safety

	SYK	BMET	ZMH
VL	2	3	2
S&P	B+	A-	NR

Financial Strength

	SYK	BMET	ZMH
VL	A	A	A
S&P	A+	A	A
M*	A+	A	A

Free Cash Flow


SYK

Cash Flow Ratios						
	1998	1999	2000	2001	2002	2003
Operating Cash Flow Growth-YOY	68.2%	83.8%	16.8%	41.1%	7.6%	28.7%
Free Cash Flow Growth-YOY	82.3%	101.2%	20.8%	22.0%	19.1%	38.1%
Cap Ex as a % of Sales	4.6%	3.6%	3.5%	6.2%	4.6%	4.0%
Free Cash Flow/Sales	9.36%	9.88%	10.97%	11.77%	12.12%	13.90%
Free Cash Flow/Net Income	2.61	10.71	1.14	1.15	1.06	1.11

FCF Growth greater than EPS is good
 FCF/S of greater than 5% is good
 FCF/Net Income greater than 1 is good
 Indicators of Quality Earnings

Source - <http://www.morningstar.com/?topnav=home>

Robertson Quality Rating

		Quality	Sales Growth	Net Margin	Finl Strength	EPS Pred
Stryker	SYK	70.9	11.6%	16.5%	80%	100
Biomet	BMET	77.8	13.7%	21.9%	80%	100
Zimmer Hldg	ZMH	69.2	13.3%	21.1%	80%	70
JNJ	JNJ	76.1	7.1%	21.0%	100%	100

RQR Quality Ratings of 65 or better are in the top quintile (20%)

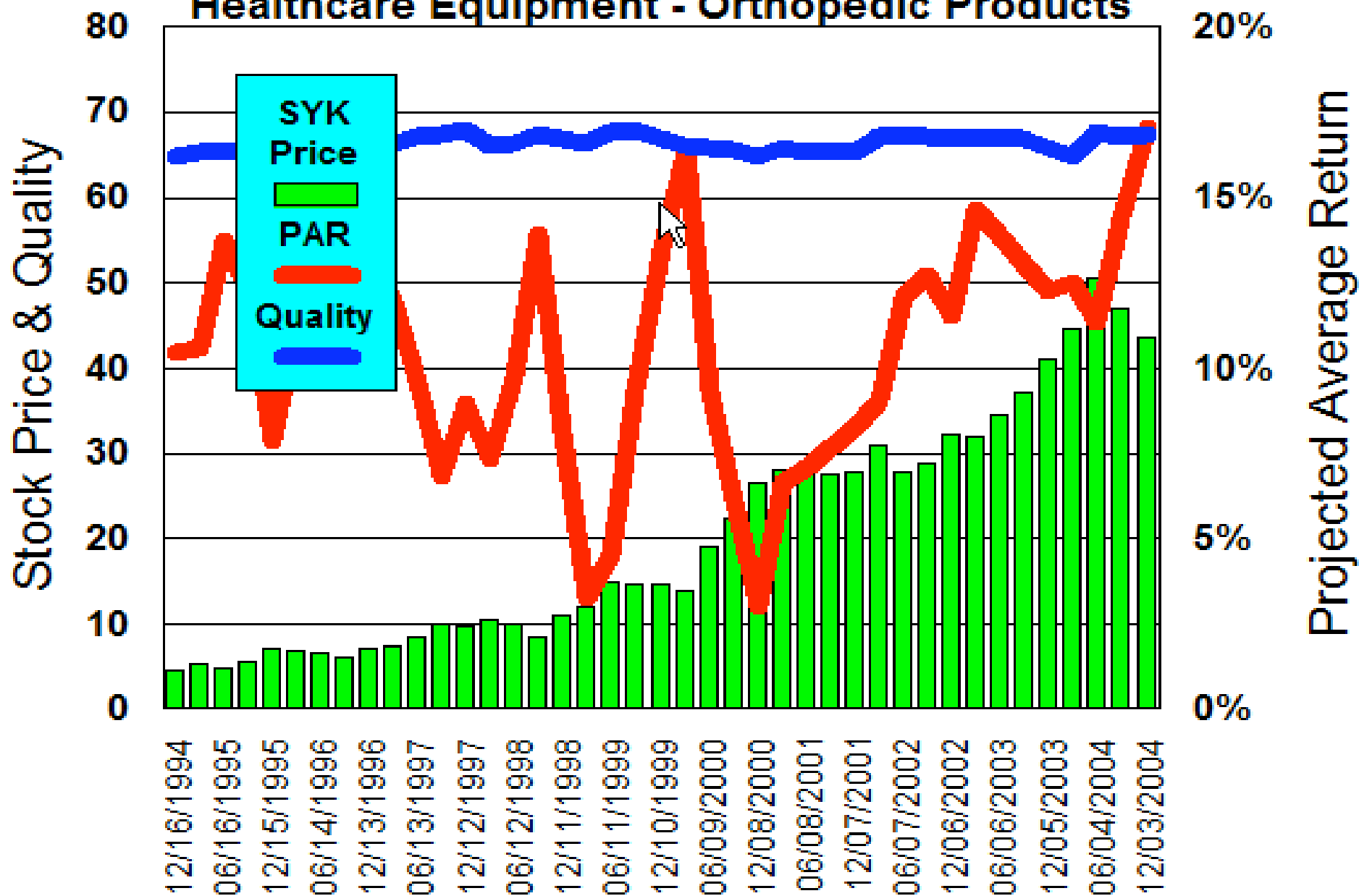
These ratings are based upon Value Line.

Our numbers may vary depending upon our judgments

• See <http://www.better-investing.org/articles/web/4654>

Stryker (SYK)

Healthcare Equipment - Orthopedic Products



View of the Industry

From Babson Staff Letter of March 12, 2004

- WW Orthopedic business in 2004 is \$15B
 - Growing at 10% per year with US even faster
- Reconstructive segment totals about 40%
 - Knees, Hips and extremities
- Spinal Implants only 14% today
 - Growing at over 20% per year

View of the Industry (cont)

The 2003 Global Orthopedic Market

Area	Percent of Market
Knees	20%
Hips	19%
Spine	14%
Trauma	12%

View of the Industry (cont)

- Favorable Long Term Trends
 - Growing of Aged Population
 - Baby Boomers push for new parts earlier
 - Growing Over Weight Population
 - Adds to joint wear and tear and need to replace

View of the Industry (cont)

Knees and Hips Global Market Share

Company	Knees	Hips
Zimmer	29%	28%
Dupuy (JNJ)	25%	22%
Stryker	19%	25%
Biomet	12%	11%
Smith & Nephew	8%	7%
Other	7%	7%

Stryker Quality Summary

- Historical Growth exceeds criteria
- Close to an industry leader
- PTPM rising – Below BMET
- ROE flat and at high level
- Industry growth & profitability strong
- Future SYK Growth = ?

Questions