

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended June 30, 2006

Commission file number: 0-9165

STRYKER CORPORATION

(Exact name of registrant as specified in its charter)

Michigan

(State or other jurisdiction of
incorporation or organization)

38-1239739

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

2725 Fairfield Road, Kalamazoo, Michigan

(Address of principal executive offices)

49002

(Zip Code)

Registrant's telephone number, including area code: **(269) 385-2600**

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

YES NO

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer

Accelerated filer

Non-accelerated filer

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act).

YES NO

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date:

406,559,317 shares of Common Stock, \$.10 par value, as of July 31, 2006.

PART I. – FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

CONDENSED CONSOLIDATED BALANCE SHEETS (Unaudited)

Stryker Corporation and Subsidiaries

(in millions, except per share amounts)

| | June 30 2006 | December 31 2005 |
|--|------------------|---------------------|
| ASSETS | | |
| <i>Current Assets</i> | | |
| Cash and cash equivalents | \$129.7 | \$491.2 |
| Marketable securities | 738.0 | 565.3 |
| Accounts receivable, less allowance of \$53.4 (\$53.4 in 2005) | 842.1 | 770.3 |
| Inventories | 644.1 | 563.5 |
| Deferred income taxes | 398.3 | 383.1 |
| Prepaid expenses and other current assets | 110.0 | 96.7 |
| Total current assets | <u>2,862.2</u> | <u>2,870.1</u> |
| <i>Property, Plant and Equipment, less allowance for depreciation of \$638.6 (\$571.5 in 2005)</i> | 892.1 | 831.0 |
| <i>Other Assets</i> | | |
| Goodwill | 522.9 | 513.2 |
| Other intangibles, less accumulated amortization of \$262.7 (\$237.5 in 2005) | 405.9 | 409.7 |
| Loaner instrumentation, less accumulated amortization of \$489.9 (\$422.3 in 2005) | 286.4 | 245.6 |
| Deferred income taxes | 103.2 | 91.1 |
| Other | 36.3 | 31.8 |
| | <u>1,354.7</u> | <u>1,291.4</u> |
| | <u>\$5,109.0</u> | <u>\$4,992.5</u> |
| LIABILITIES AND SHAREHOLDERS' EQUITY | | |
| <i>Current Liabilities</i> | | |
| Accounts payable | \$193.3 | \$206.5 |
| Accrued compensation | 209.6 | 252.9 |
| Income taxes | 177.4 | 207.3 |
| Accrued expenses and other liabilities | 464.2 | 534.7 |
| Current maturities of long-term debt | 13.5 | 47.4 |
| Total current liabilities | <u>1,058.0</u> | <u>1,248.8</u> |
| <i>Long-Term Debt, excluding current maturities</i> | 0.7 | 184.2 |
| <i>Other Liabilities</i> | 281.2 | 259.3 |
| <i>Shareholders' Equity</i> | | |
| Common stock, \$.10 par value: | | |
| Authorized - 1,000.0 shares | | |
| Outstanding - 406.5 shares (405.2 in 2005) | 40.6 | 40.5 |
| Additional paid-in capital | 511.4 | 452.0 |
| Retained earnings | 3,163.9 | 2,802.5 |
| Accumulated other comprehensive gain | 53.2 | 5.2 |
| Total shareholders' equity | <u>3,769.1</u> | <u>3,300.2</u> |
| | <u>\$5,109.0</u> | <u>\$4,992.5</u> |

See accompanying notes to condensed consolidated financial statements.

CONDENSED CONSOLIDATED STATEMENTS OF EARNINGS (Unaudited)

Stryker Corporation and Subsidiaries

(in millions, except per share amounts)

| | Three Months Ended | | Six Months Ended | |
|--|--------------------|-----------|------------------|-----------|
| | June 30 | | June 30 | |
| | 2006 | 2005 | 2006 | 2005 |
| Net sales | \$1,327.9 | \$1,218.6 | \$2,648.8 | \$2,421.1 |
| Cost of sales | 452.5 | 423.1 | 905.4 | 853.1 |
| Gross profit | 875.4 | 795.5 | 1,743.4 | 1,568.0 |
| Research, development and engineering expenses | 75.9 | 67.0 | 153.0 | 128.6 |
| Selling, general and administrative expenses | 497.0 | 465.6 | 1,002.7 | 923.7 |
| Intangibles amortization | 10.6 | 11.4 | 21.0 | 27.8 |
| Purchased in-process research and development | -- | -- | 52.7 | -- |
| | 583.5 | 544.0 | 1,229.4 | 1,080.1 |
| Operating income | 291.9 | 251.5 | 514.0 | 487.9 |
| Other income (expense) | 4.7 | (0.2) | 9.9 | (0.8) |
| Earnings before income taxes | 296.6 | 251.3 | 523.9 | 487.1 |
| Income taxes | 82.7 | 73.5 | 162.5 | 142.6 |
| Net earnings | \$213.9 | \$177.8 | \$361.4 | \$344.5 |
| Net earnings per share of common stock: | | | | |
| Basic | \$.53 | \$.44 | \$.89 | \$.85 |
| Diluted | \$.52 | \$.43 | \$.88 | \$.84 |
| Average outstanding shares for the period: | | | | |
| Basic | 406.4 | 403.3 | 406.0 | 403.1 |
| Diluted | 410.7 | 410.5 | 411.0 | 410.7 |

See accompanying notes to condensed consolidated financial statements.

CONDENSED CONSOLIDATED STATEMENT OF SHAREHOLDERS' EQUITY (Unaudited)

Stryker Corporation and Subsidiaries

(in millions, except per share amounts)

| | Common Stock | Additional Paid-In Capital | Retained Earnings | Accumulated Other Comprehensive Gain (Loss) | Total |
|---|-----------------|----------------------------------|----------------------|--|-----------|
| Balances at January 1, 2006 | \$40.5 | \$452.0 | \$2,802.5 | \$5.2 | \$3,300.2 |
| Net earnings | -- | -- | 361.4 | -- | 361.4 |
| Unrealized losses on securities | -- | -- | -- | (2.4) | (2.4) |
| Unfunded pension losses | -- | -- | -- | (0.3) | (0.3) |
| Foreign currency translation adjustments | -- | -- | -- | 50.7 | 50.7 |
| Comprehensive earnings for the six months ended June 30, 2006 | | | | | 409.4 |
| Issuance of 1.3 shares of common stock under stock option and benefit plans, including \$13.7 excess income tax benefit | 0.1 | 30.1 | -- | -- | 30.2 |
| Share-based compensation | -- | 29.3 | -- | -- | 29.3 |
| Balances at June 30, 2006 | \$40.6 | \$511.4 | \$3,163.9 | \$53.2 | \$3,769.1 |

See accompanying notes to condensed consolidated financial statements.

In 2005, the Company declared a cash dividend of eleven cents per share to shareholders of record on December 30, 2005, payable on January 31, 2006. No cash dividends have been declared during 2006.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)

Stryker Corporation and Subsidiaries

(in millions)

| | Three Months Ended | | Six Months Ended | |
|---|--------------------|-----------|------------------|-----------|
| | June 30 | | June 30 | |
| | 2006 | 2005 | 2006 | 2005 |
| <i>Operating Activities</i> | | | | |
| Net earnings | \$213.9 | \$177.8 | \$361.4 | \$344.5 |
| Adjustments to reconcile net earnings to net cash provided by operating activities: | | | | |
| Depreciation | 30.4 | 26.4 | 59.1 | 53.5 |
| Amortization | 51.5 | 43.0 | 100.6 | 89.8 |
| Share-based compensation | 14.3 | 10.2 | 29.3 | 20.2 |
| Income tax benefit from exercise of stock options | 4.7 | 5.8 | 16.6 | 12.3 |
| Excess income tax benefit from exercise of stock options | (3.8) | (5.0) | (13.7) | (10.6) |
| Purchased in-process research and development | -- | -- | 52.7 | -- |
| Other | 1.3 | 1.5 | 4.1 | 3.8 |
| Changes in operating assets and liabilities, net of effects of acquisitions: | | | | |
| Accounts receivable | 14.2 | (1.9) | (56.3) | (29.2) |
| Inventories | (37.4) | (34.0) | (68.1) | (46.6) |
| Loaner instrumentation | (58.7) | (54.3) | (116.8) | (109.2) |
| Accounts payable | (12.3) | 8.4 | (17.7) | (30.0) |
| Accrued expenses | 24.8 | 54.5 | (64.4) | (8.3) |
| Income taxes | (58.8) | (59.0) | (44.7) | (85.1) |
| Other | 11.7 | 8.8 | (25.6) | 3.5 |
| Net cash provided by operating activities | 195.8 | 182.2 | 216.5 | 208.6 |
| <i>Investing Activities</i> | | | | |
| Acquisitions, net of cash acquired | (31.9) | (3.0) | (79.3) | (53.1) |
| Purchases of marketable securities | (3,257.5) | (212.9) | (3,673.7) | (212.9) |
| Proceeds from sales of marketable securities | 3,195.2 | -- | 3,501.0 | -- |
| Purchases of property, plant and equipment | (52.3) | (71.1) | (104.2) | (116.4) |
| Proceeds from sales of property, plant and equipment | 0.1 | 0.2 | 0.2 | 0.4 |
| Net cash used in investing activities | (146.4) | (286.8) | (356.0) | (382.0) |
| <i>Financing Activities</i> | | | | |
| Proceeds from borrowings | 73.1 | 198.1 | 84.8 | 246.7 |
| Payments on borrowings | (201.8) | (197.9) | (311.6) | (246.5) |
| Dividends paid | -- | -- | (44.6) | (36.2) |
| Proceeds from exercise of stock options | 5.9 | 5.8 | 19.5 | 11.7 |
| Excess income tax benefit from exercise of stock options | 3.8 | 5.0 | 13.7 | 10.6 |
| Other | (1.6) | (17.2) | 13.1 | (27.2) |
| Net cash used in financing activities | (120.6) | (6.2) | (225.1) | (40.9) |
| Effect of exchange rate changes on cash and cash equivalents | 2.5 | (15.5) | 3.1 | (16.7) |
| Decrease in cash and cash equivalents | (\$68.7) | (\$126.3) | (\$361.5) | (\$231.0) |

See accompanying notes to condensed consolidated financial statements.

NOTE 1
BASIS OF PRESENTATION

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by United States generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. The results of operations for the six-months ended June 30, 2006 are not necessarily indicative of the results that may be expected for the year ended December 31, 2006.

The balance sheet at December 31, 2005 has been derived from the audited financial statements at that date, after adjustments to deferred income taxes and shareholders' equity balances made pursuant to the adoption of Financial Accounting Standards Board (FASB) Statement No. 123 (revised), *Share-Based Payment*; but does not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements.

For further information, refer to the consolidated financial statements and footnotes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2005 (the "2005 Form 10-K").

Effective January 1, 2006, the Company adopted the provisions of FASB Statement No. 123 (revised). The revised Statement supersedes Accounting Principles Board (APB) Opinion No. 25, *Accounting for Stock Issued to Employees*, and its related implementation guidance. Under Opinion No. 25, no compensation expense was recognized for the cost of stock options granted pursuant to the Company's key employee and director stock option plans because the exercise price of the Company's stock options was equal to the market price of the underlying stock on the measurement date (date of grant). The revised Statement requires companies to recognize the cost of stock options based on the grant-date fair value determined under their employee stock option plans over the period during which the recipient is required to provide services in exchange for the options, typically the vesting period. The Company adopted the provisions of the revised Statement using the modified-retrospective transition method provided in the revised Statement. Under this method, the Company restated all prior periods presented on a consistent basis, based on the pro forma expense previously disclosed.

As a result of the adoption of the revised Statement, the Company's operating income for the first half of 2006 and 2005 was reduced by \$29.0 million and \$19.9 million, respectively, and the Company's net earnings for the same periods were reduced by \$18.8 million and \$12.9 million, respectively. Basic net earnings per share for the first half of 2006 and 2005 were reduced by \$.05 and \$.03, respectively, and diluted net earnings per share were reduced by \$.05 and \$.03, respectively. The Company's operating income for the second quarter of 2006 and 2005 was reduced by \$14.2 million and \$10.1 million, respectively, and the Company's net earnings for the same periods were reduced by \$9.2 million and \$6.5 million, respectively. Basic and diluted net earnings per share for the second quarter of both 2006 and 2005 were reduced by \$.02. In addition, prior period balance sheets have been adjusted to reflect the cumulative impact of stock option compensation expense and stock option exercise activity as required by the modified-retrospective transition method. The balance sheet at December 31, 2005 was adjusted to reflect decreases in retained earnings and deferred stock-based compensation of \$125.7 million and \$1.6 million, respectively, and increases in the balances of additional paid-in capital and noncurrent deferred income tax assets of \$172.5 million and \$48.4 million, respectively.

Prior to the adoption of the revised Statement, the Company presented all of the income tax benefits resulting from the exercise of stock options as cash flows provided by operating activities in the condensed consolidated statements of cash flows. The revised Statement requires the income tax benefit from deductions, resulting from the exercise of stock options, in excess of the compensation cost recognized (excess income tax benefit) to be classified as cash flows provided by financing activities. The \$13.7 million and \$10.6 million excess income tax benefit from exercise of stock options reported as cash flows provided by financing activities for the first half of 2006 and 2005, respectively, would have been

classified as cash flows provided by operating activities if the Company had not adopted the provisions of the revised Statement.

In June 2006, the FASB issued Interpretation No. 48, *Accounting for Uncertainty in Income Taxes, an Interpretation of FASB Statement No. 109*. This Interpretation clarifies the accounting for income taxes by prescribing the minimum recognition threshold a tax position is required to meet before being recognized in the financial statements. The Interpretation also provides guidance for the measurement and classification of tax positions, interest and penalties, and requires additional disclosure on an annual basis. The Company plans to adopt the provisions of the Interpretation effective January 1, 2007, as required. The Company has not yet determined what effect the adoption of the Interpretation will have on net earnings, net earnings per share and the financial position of the Company, however, any difference between the amounts recognized in the Company's financial statements prior to the adoption of the Interpretation and the amounts reported after the adoption will be accounted for as a cumulative-effect adjustment recorded in the beginning balance of retained earnings and will not require restatement of prior periods.

NOTE 2 COMPREHENSIVE EARNINGS

The Company follows FASB Statement No. 130, *Reporting Comprehensive Income*, in accounting for comprehensive earnings and its components. The comprehensive earnings for the six months ended June 30, 2006 and 2005 were \$409.4 million and \$197.4 million, respectively, and for the three months ended June 30, 2006 and 2005 were \$258.5 million and \$79.1 million, respectively.

NOTE 3 INVENTORIES

Inventories are as follows (in millions):

| | June 30 | December 31 |
|-------------------|----------------|----------------|
| | 2006 | 2005 |
| Finished goods | \$471.7 | \$414.9 |
| Work-in-process | 77.5 | 65.4 |
| Raw material | 98.7 | 87.0 |
| FIFO Cost | 647.9 | 567.3 |
| Less LIFO reserve | 3.8 | 3.8 |
| | <u>\$644.1</u> | <u>\$563.5</u> |

NOTE 4 ACQUISITIONS

In the first quarter of 2006, the Company acquired all of the outstanding stock of Sightline Technologies Ltd. (Sightline), a private, development-stage company, for an upfront payment of \$50.0 million in cash plus certain transaction costs and the assumption of certain liabilities. The acquisition of Sightline, a developer of flexible endoscopes, is expected to enhance the Company's presence in the gastrointestinal and other markets within its MedSurg Equipment segment. Sightline's operating results are included in the Company's condensed consolidated financial statements from the date of the acquisition and are not material to the Company's operating results. Pro forma consolidated results of operations would not differ significantly as a result of the Sightline acquisition.

The purchase price has been preliminarily allocated to assets acquired, purchased in-process research and development and liabilities assumed based on their estimated fair value at the date of acquisition. The amount of the purchase price allocated to purchased in-process research and development resulted in a charge of \$52.7 million, or \$.13

per diluted share, against the Company's first quarter operating results. At the date of the acquisition, the flexible endoscope technologies acquired had not yet reached technological feasibility. The amount written-off as purchased in-process research and development will not be deductible for income tax purposes.

Terms of the transaction also include potential milestone payments of up to an additional \$90.0 million upon the achievement of certain operational and financial targets related to Sightline's products, the first of which is not expected to occur before 2007. The potential milestone payments are expected to be capitalized at their fair values as intangible assets at the time of payment and will be amortized over their remaining useful lives.

NOTE 5

CAPITAL STOCK AND NET EARNINGS PER SHARE

The Company has key employee and director stock option plans under which options are granted at an exercise price not less than the fair market value of the underlying common stock 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 (in millions) | Weighted-Average Exercise Price | Weighted-Average Remaining Contractual Term (in years) | Aggregate Intrinsic Value (in millions) |
|--|-------------------------|------------------------------------|---|---|
| Options outstanding at January 1, 2006 | 24.2 | \$28.78 | | |
| Granted | 4.7 | 46.84 | | |
| Exercised | (1.4) | 14.11 | | |
| Cancelled | <u>(0.2)</u> | 43.73 | | |
| Options outstanding at June 30, 2006 | <u>27.3</u> | \$32.55 | 6.5 | \$312.9 |
| Exercisable at June 30, 2006 | 14.9 | \$23.54 | 4.9 | \$284.4 |
| Options expected to vest | 11.6 | \$43.00 | 8.3 | \$29.7 |

The aggregate intrinsic value of options exercised during the six months ended June 30, 2006 and 2005 were \$46.3 million and \$35.6 million, respectively. Shares reserved for future compensation grants of Stryker Common Stock were 25.6 million at June 30, 2006. Option shares reserved for future grants were 10.1 million at December 31, 2005. Exercise prices for options outstanding as of June 30, 2006 ranged from \$7.10 to \$48.27. At June 30, 2006, there was \$162.3 million of unrecognized compensation cost related to nonvested stock options granted under the stock option plans; that cost is expected to be recognized over the following 8.7 years (weighted-average period of 2.1 years).

A summary of nonvested option activity follows (in millions, except per share amounts):

| | Shares | Weighted-Average Grant-Date Fair Value |
|------------------------------|--------------|--|
| Nonvested at January 1, 2006 | 9.8 | \$15.59 |
| Granted | 4.7 | 17.16 |
| Vested | (1.9) | 15.21 |
| Cancelled | <u>(0.2)</u> | 16.10 |
| Nonvested at June 30, 2006 | <u>12.4</u> | \$16.24 |

The grant-date fair values of options granted during the six months ended June 30, 2006 using the Black-Scholes option pricing model were estimated using the following weighted-average assumptions:

| | |
|---------------------------------|-------------|
| | <u>2006</u> |
| Risk-free interest rate | 4.6% |
| Expected dividend yield | 0.2% |
| Expected stock price volatility | 24.8% |
| Expected option life | 7.0 years |

The risk-free interest rate for periods within the expected life of the option is based on the U.S. Treasury yield curve in effect at the time of grant. Expected volatilities are based on historical volatility of the Company's stock. The Company uses historical data to estimate option exercise and employee termination within the valuation model. The expected option life is derived from the output of the option valuation model and represents the period of time that options granted are expected to be outstanding.

Options to purchase an average of 7.2 million and 1.7 million shares of common stock during the six months ended June 30, 2006 and 2005, respectively, and 11.0 million and 3.4 million shares of common stock during the three months ended June 30, 2006 and 2005, respectively, were outstanding but were not included in the computation of diluted net earnings per share because the exercise prices of the options were greater than the average market price of common shares for those periods.

NOTE 6 RETIREMENT PLANS

Certain of the Company's subsidiaries have both funded and unfunded defined benefit plans covering some or all of their employees. The components of net periodic benefit cost are as follows (in millions):

| | Three Months Ended | | Six Months Ended | |
|---|--------------------|--------------|------------------|--------------|
| | June 30 | | June 30 | |
| | 2006 | 2005 | 2006 | 2005 |
| Service cost | \$2.7 | \$2.3 | \$5.5 | \$4.4 |
| Interest cost | 2.2 | 1.6 | 3.5 | 3.2 |
| Expected return on plan assets | (2.0) | (1.3) | (2.9) | (2.5) |
| Amortization of transition amounts and prior service cost | 0.1 | 0.2 | 0.2 | 0.4 |
| Recognized actuarial loss | 0.4 | 0.1 | 0.6 | 0.2 |
| Net periodic benefit cost | <u>\$3.4</u> | <u>\$2.9</u> | <u>\$6.9</u> | <u>\$5.7</u> |

The Company previously disclosed in its 2005 Form 10-K that it anticipated contributing approximately \$9.2 million to its defined benefit plans in 2006 to meet minimum funding requirements. As of June 30, 2006, \$2.3 million of contributions have been made.

NOTE 7 SEGMENT INFORMATION

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, spinal and craniomaxillofacial implant systems; bone cement; and the bone growth factor OP-1. The MedSurg Equipment segment sells surgical equipment; surgical navigation systems; endoscopic, communications, and digital imaging systems; as well as patient handling and emergency medical equipment. The Other category includes Physical Therapy Services and corporate administration, interest expense and interest income.

Effective January 1, 2006, the Company changed its business segment reporting to include the financial results of certain products within its MedSurg Equipment segment rather than within its Orthopaedic Implants segment. The Company believes these products are better aggregated with its other MedSurg Equipment products based on similarities in manufacturing and marketing practices and customer base.

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 found in Note 1 of the Company's 2005 Form 10-K. The Company measures the financial results of its reportable segments using an internal performance measure that excludes the purchased in-process research and development charge recognized for the Sightline acquisition as well as the effect of share based compensation, which includes compensation related to both employee and director stock option plans and restricted stock grants.

Sales and net earnings (loss) by business segment follow (in millions):

| | Orthopaedic Implants | MedSurg Equipment | Other | Total |
|--|-------------------------|----------------------|---------|----------------|
| <u>Three Months Ended June 30, 2006</u> | | | | |
| Net sales | \$771.1 | \$490.7 | \$66.1 | \$1,327.9 |
| Segment net earnings (loss) | 151.8 | 74.8 | (3.4) | 223.2 |
| Less share-based compensation | | | | 9.3 |
| Net earnings | | | | <u>\$213.9</u> |
| <u>Three Months Ended June 30, 2005</u> | | | | |
| Net sales | \$723.5 | \$428.7 | \$66.4 | \$1,218.6 |
| Segment net earnings (loss) | 124.4 | 66.6 | (6.6) | 184.4 |
| Less share-based compensation | | | | 6.6 |
| Net earnings | | | | <u>\$177.8</u> |
| <u>Six Months Ended June 30, 2006</u> | | | | |
| Net sales | \$1,534.7 | \$981.0 | \$133.1 | \$2,648.8 |
| Segment net earnings (loss) | 290.0 | 149.3 | (6.2) | 433.1 |
| Less purchased in-process research and development | | | | 52.7 |
| Less share-based compensation | | | | 19.0 |
| Net earnings | | | | <u>\$361.4</u> |
| <u>Six Months Ended June 30, 2005</u> | | | | |
| Net sales | \$1,436.5 | \$853.1 | \$131.5 | \$2,421.1 |
| Segment net earnings (loss) | 239.9 | 128.3 | (10.6) | 357.6 |
| Less share-based compensation | | | | 13.1 |
| Net earnings | | | | <u>\$344.5</u> |

NOTE 8 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, intellectual property 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 condensed consolidated financial statements.

In December 2003, the Company announced that its subsidiary Physiotherapy Associates, Inc., and Stryker received a subpoena from the United States Attorney's Office in Boston, Massachusetts, in connection with a Department of Justice investigation of Physiotherapy Associates' billing and coding practices. In March 2005, the Company announced that it received a subpoena from the United States Department of Justice requesting documents for the period January 2002 through the present relating to "any and all consulting contracts, professional service agreements, or remuneration agreements between Stryker Corporation and any orthopedic surgeon, orthopedic surgeon in training, or medical school graduate using or considering the surgical use of hip or knee joint replacement/reconstruction products manufactured or sold by Stryker Corporation." In June 2006, the Company announced that it received a subpoena from the United States Department of Justice, Antitrust Division requesting documents for the period January 2001 through the present regarding possible violations of federal criminal law, including possible violation of the antitrust laws, relating to the manufacture and sale of orthopaedic implant devices. The Company is fully cooperating with the Department of Justice regarding these matters.

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

Executive Level Overview

Stryker Corporation (the Company or Stryker) is one of the world's leading medical technology companies with the most broadly based range of products in orthopaedics and a significant presence in other medical specialties. Stryker works with respected medical professionals to help people lead more active and more satisfying lives. The Company's products include implants used in joint replacement, trauma, craniomaxillofacial and spinal surgeries; biologics; surgical, neurologic, ear, nose & throat and interventional pain equipment; endoscopic, surgical navigation, communications and digital imaging systems; as well as patient handling and emergency medical equipment. Stryker also provides outpatient physical therapy services in the United States.

Domestic sales accounted for 65% of total revenues in the first half and second quarter of 2006 compared to 64% for the same periods in 2005. Most of the Company's products are marketed directly to more than 6,000 hospitals and to doctors and other health-care facilities. Stryker primarily maintains separate and dedicated sales forces for each of its principal product lines to provide focus and a high level of expertise to each medical specialty served.

International sales accounted for 35% of total revenues in the first half and second quarter of 2006 compared to 36% for the same periods in 2005. The Company's products are sold in more than 100 countries through both Company owned sales subsidiaries and branches and third-party dealers and distributors.

The Company's business is generally not seasonal in nature; however, the number of orthopaedic implant surgeries is lower during the summer months.

Effective January 1, 2006 the Company adopted the provisions of Financial Accounting Standards Board (FASB) Statement No. 123 (revised), *Share-Based Payment*. The revised Statement supersedes Accounting Principles Board (APB) Opinion No. 25, *Accounting for Stock Issued to Employees*, and its related implementation guidance. Under Opinion No. 25, no compensation expense was recognized for the cost of stock options granted pursuant to the Company's key employee and director stock option plans because the exercise price of the Company's stock options was equal to the market price of the underlying stock on the measurement date (date of grant). The revised Statement requires companies to recognize the cost of stock options based on the grant-date fair value determined under their employee stock option plans over the period during which the recipient is required to provide services in exchange for the options, typically the vesting period. The Company adopted the provisions of the revised Statement using the modified-retrospective transition method provided in the revised Statement. Under this method, the Company restated all prior periods presented on a consistent basis, based on the pro forma expense previously disclosed. Additional details, including the financial statement impact resulting from this adoption, are included in *Results of Operations*.

Outlook

The Company's outlook for 2006 continues to be optimistic regarding underlying growth rates in orthopaedic procedures and the Company's broadly based range of products in orthopaedics and other medical specialties, despite the potential for increased pricing pressure on Orthopaedic Implants products in the United States, Japan and certain other foreign markets. The Company projects adjusted diluted net earnings per share for 2006 of \$2.02, excluding the impact of the charge to write off purchased in-process research and development associated with the acquisition of Sightline during the first quarter of 2006. The projection represents a 21.0% increase over adjusted restated diluted net earnings per share of \$1.67 in 2005.

The financial forecast for 2006 includes a net sales increase in the range of 11% to 13% as a result of growth in shipments of Orthopaedic Implants and MedSurg Equipment and higher revenue from Physical Therapy Services, offset by unfavorable foreign currency exchange rate movements. If foreign currency exchange rates hold near recent levels, the Company does not expect a significant impact on net sales in the third quarter and anticipates an unfavorable impact of 0% to 1% for the full year of 2006. Excluding the effect of foreign currency exchange rates, the Company expects annual net sales growth in the range of 11% to 13% in 2006, which is comparable to the 11% sales growth, excluding the effect of foreign currency exchange rates, reported for the first half of 2006.

Results of Operations

The tables below outline the components of the condensed consolidated statements of earnings as a percentage of net sales and the period-to-period percentage change in dollar amounts:

| | <u>Percentage of Net Sales</u> | | |
|--|--------------------------------|-------|------------|
| | Six Months Ended | | Percentage |
| | June 30 | | Change |
| | 2006 | 2005 | 2006/2005 |
| Net sales | 100.0 | 100.0 | 9% |
| Cost of sales | 34.2 | 35.2 | 6 |
| Gross profit | 65.8 | 64.8 | 11 |
| Research, development and engineering expenses | 5.8 | 5.3 | 19 |
| Selling, general and administrative expenses | 37.9 | 38.2 | 9 |
| Intangibles amortization | 0.8 | 1.1 | (24) |
| Purchased in-process research and development | 2.0 | -- | -- |
| Operating income | 19.4 | 20.2 | 5 |
| Other income (expense) | 0.4 | -- | -- |
| Earnings before income taxes | 19.8 | 20.1 | 8 |
| Income taxes | 6.1 | 5.9 | 14 |
| Net earnings | 13.6 | 14.2 | 5 |

| | <u>Percentage of Net Sales</u> | | Percentage Change |
|--|--------------------------------|-------|----------------------|
| | Three Months Ended | | |
| | 2006 | 2005 | 2006/2005 |
| Net sales | 100.0 | 100.0 | 9% |
| Cost of sales | 34.1 | 34.7 | 7 |
| Gross profit | 65.9 | 65.3 | 10 |
| Research, development and engineering expenses | 5.7 | 5.5 | 13 |
| Selling, general and administrative expenses | 37.4 | 38.2 | 7 |
| Intangibles amortization | 0.8 | 0.9 | (7) |
| Operating income | 22.0 | 20.6 | 16 |
| Other income (expense) | 0.4 | -- | -- |
| Earnings before income taxes | 22.3 | 20.6 | 18 |
| Income taxes | 6.2 | 6.0 | 13 |
| Net earnings | 16.1 | 14.6 | 20 |

The tables below set forth domestic/international and product line sales information (in millions):

| | Six Months Ended | | Percentage Change | |
|------------------------------|------------------|------------------|-------------------|----------------------|
| | June 30 | | 2006/2005 | |
| | 2006 | 2005 | Reported | Constant Currency |
| Domestic/international sales | | | | |
| Domestic | \$1,731.9 | \$1,558.8 | 11% | 11% |
| International | 916.9 | 862.3 | 6 | 10 |
| Total net sales | <u>\$2,648.8</u> | <u>\$2,421.1</u> | 9 | 11 |
| Product line sales | | | | |
| Orthopaedic Implants | \$1,534.7 | \$1,436.5 | 7 | 9 |
| MedSurg Equipment | 981.0 | 853.1 | 15 | 16 |
| Physical Therapy Services | 133.1 | 131.5 | 1 | 1 |
| Total net sales | <u>\$2,648.8</u> | <u>\$2,421.1</u> | 9 | 11 |

| | Three Months Ended June 30 | | Percentage Change | |
|------------------------------|-------------------------------|------------------|-------------------|----------------------|
| | | | 2006/2005 | |
| | 2006 | 2005 | Reported | Constant Currency |
| Domestic/international sales | | | | |
| Domestic | \$864.0 | \$784.1 | 10% | 10% |
| International | 463.9 | 434.5 | 7 | 8 |
| Total net sales | <u>\$1,327.9</u> | <u>\$1,218.6</u> | 9 | 9 |
| Product line sales | | | | |
| Orthopaedic Implants | \$771.1 | \$723.5 | 7 | 7 |
| MedSurg Equipment | 490.7 | 428.7 | 14 | 14 |
| Physical Therapy Services | 66.1 | 66.4 | -- | -- |
| Total net sales | <u>\$1,327.9</u> | <u>\$1,218.6</u> | 9 | 9 |

The tables below set forth additional sales growth information for significant products within the Company's Orthopaedic Implants and MedSurg Equipment segments on both a reported basis and a constant currency basis that excludes the impact of changes in foreign currency exchange rates:

| | <u>Percentage Change</u> | |
|---|--------------------------|------------------------------|
| | Six Months Ended | |
| | June 30 | |
| | <u>2006/2005</u> | |
| | <u>Reported</u> | <u>Constant Currency</u> |
| Worldwide Orthopaedic Implants sales: | | |
| Hips | 0% | 2% |
| Knees | 11 | 13 |
| Trauma | 10 | 14 |
| Spine | 16 | 17 |
| Craniofacial | 8 | 9 |
| Worldwide MedSurg Equipment sales: | | |
| Surgical equipment and surgical navigation systems | 13 | 14 |
| Endoscopic, communications and digital imaging systems | 14 | 15 |
| Patient handling and emergency medical equipment | 20 | 19 |

Percentage Change
Three Months Ended
June 30
2006/2005
Constant
Reported Currency

Worldwide Orthopaedic Implants sales:

| | | |
|----------------|----|----|
| Hips | 0% | 0% |
| Knees | 10 | 10 |
| Trauma | 11 | 13 |
| Spine | 13 | 14 |
| Micro implants | 8 | 8 |

Worldwide MedSurg Equipment sales:

| | | |
|--|----|----|
| Surgical equipment and surgical navigation systems | 12 | 12 |
| Endoscopic, communications and digital imaging systems | 13 | 13 |
| Patient handling and emergency medical equipment | 23 | 22 |

Stryker Corporation's net sales increased 9% in the first half of 2006 to \$2,648.8 million from \$2,421.1 million in 2005. For the second quarter of 2006 net sales were \$1,327.9 million, representing a 9% increase over net sales of \$1,218.6 million in the second quarter of 2005. Net sales for the first half of 2006 grew by 10% as a result of increased unit volume and changes in product mix partially offset by an unfavorable impact on net sales growth of 1% due to changes in foreign currency exchange rates. Net sales for the second quarter of 2006 grew by 9% as a result of increased unit volume and changes in product mix.

The Company's domestic sales were \$1,731.9 million for the first half of 2006 and \$864.0 million for the second quarter of 2006, representing increases of 11% and 10%, respectively, as a result of higher shipments of Orthopaedic Implants and MedSurg Equipment. International sales were \$916.9 million for the first half of 2006 and \$463.9 million for the second quarter of 2006, representing increases of 6% and 7%, respectively, as a result of higher shipments of Orthopaedic Implants and MedSurg Equipment. The impact of foreign currency comparisons to the dollar value of international sales was unfavorable by \$34.8 million in the first half and by \$4.9 million in the second quarter. Excluding the impact of foreign currency, international sales increased 10% in the first half of 2006 and 8% in the second quarter of 2006.

Worldwide sales of Orthopaedic Implants were \$1,534.7 million for the first half of 2006 and \$771.1 million for the second quarter of 2006, representing increases of 7% for both periods as a result of higher shipments of reconstructive (hip, knee and shoulder), trauma, spinal and craniomaxillofacial implant systems; bone cement; and the bone growth factor OP-1. Excluding the impact of foreign currency, sales of Orthopaedic Implants increased 9% in the first half of 2006 and 7% in the second quarter of 2006. Comparative quarterly sales of Orthopaedic Implants can be positively or negatively impacted by the number of business days available during the quarter to perform surgeries. Comparative Orthopaedic Implant sales for the second quarter of 2006 were negatively impacted by one fewer business day in the United States and two fewer business days in Europe.

Sales of hip implant systems were flat in both the first half and the second quarter of 2006 (up 2% and flat, respectively, excluding changes in foreign currency exchange rates). In the United States, sales growth was driven by sales of the recently launched X3 Polyethylene and sales growth in Accolade cementless hip products and Restoration Modular Hip System revision hip products partially offset by declines in other hip systems. Solid growth in the Trident

Hip System in Europe and Accolade cementless hip products in the Pacific region also led to the Company's constant currency sales growth for the first half of 2006.

Sales of knee implant systems increased 11% in the first half of 2006 and 10% in the second quarter (13% and 10%, respectively, excluding changes in foreign currency exchange rates) due to strong growth in the Triathlon knee system in the United States and solid growth in the Triathlon and Scorpio knee systems in international markets.

Sales of trauma implant systems increased 10% in the first half of 2006 and 11% in the second quarter (14% and 13%, respectively, excluding changes in foreign currency exchange rates) as a result of strong sales growth in the T2 Nailing system in the United States and Europe as well as solid sales growth in the Gamma 3 Hip Fracture System in the United States.

Sales of spinal implant systems increased 16% in the first half of 2006 and 13% in the second quarter (17% and 14%, respectively, excluding changes in foreign currency exchange rates) primarily due to strong sales growth of interbody devices in the United States led by sales of the AVS vertebral spacer system.

Sales of craniomaxillofacial implant systems increased 8% in both the first half and second quarter of 2006 (9% and 8%, respectively, excluding changes in foreign currency exchange rates) as a result of strong domestic sales growth led by products for neurological indications.

Worldwide sales of MedSurg Equipment were \$981.0 million for the first half of 2006 and \$490.7 million for the second quarter of 2006, representing increases of 15% and 14%, respectively, as a result of higher shipments of surgical equipment; surgical navigation systems; endoscopic, communications and digital imaging systems; as well as patient handling and emergency medical equipment. Excluding the impact of foreign currency, sales of MedSurg Equipment increased 16% and 14% for the first half and second quarter of 2006, respectively.

Sales of surgical equipment and surgical navigation systems increased 13% in the first half of 2006 and 12% in the second quarter (14% and 12%, respectively, excluding changes in foreign currency exchange rates) due to strong domestic sales growth in surgical navigation systems, operating room equipment and interventional pain products. Strong sales growth in powered surgical instruments outside the United States also led to the Company's constant currency sales growth.

Sales of endoscopic, communications and digital imaging systems increased 14% in the first half of 2006 and 13% in the second quarter (15% and 13%, respectively, excluding changes in foreign currency exchange rates) as a result of strong worldwide sales growth in general surgery products and very solid worldwide sales growth in medical video imaging equipment led by image portal and communications products. Strong growth in arthroscopy products in Europe also drove sales in the first half of the year.

Sales of patient handling and emergency medical equipment increased 20% in the first half of 2006 and 23% in the second quarter (19% and 22%, respectively, excluding changes in foreign currency exchange rates) due to strong sales growth in bed products in the United States and Latin America and strong domestic sales growth in emergency medical equipment.

Physical Therapy Services revenues were \$133.1 million for first half of 2006 and \$66.1 for the second quarter of 2006, representing an increase of 1% for the first half of 2006 and flat year over year sales in the second quarter, with all of the growth for the year coming from new physical therapy centers.

Cost of sales in the first half of 2006 represented 34.2% of sales compared to 35.2% in the same period of 2005. In the second quarter of 2006, the cost of sales percentage decreased to 34.1% from 34.7% in the second quarter of 2005. The decrease in the cost of sales percentage is primarily due to lower excess and obsolete inventory costs as a result of fewer comparative product introductions in the first half of 2006, partially offset by faster sales growth in the lower margin MedSurg Equipment.

Research, development and engineering expenses represented 5.8% of sales in the first half of 2006 compared to 5.3% in the same period of 2005 and increased 19% to \$153.0 million. In the second quarter these costs increased 13% and represented 5.7% of sales in 2006 compared to 5.5% in 2005. The higher spending level is the result of the Company's continued focus on new product development for anticipated product launches throughout the remainder of the year and in future years.

Selling, general and administrative expenses increased 9% in the first half of 2006 and represented 37.9% of sales compared to 38.2% in the same period of 2005. In the second quarter, these expenses increased 7% and represented 37.4% of sales in 2006 compared to 38.2% in 2005. The decrease in selling, general and administrative expenses as a percent of sales in the first half and for the second quarter of 2006 is primarily due to decreases in insurance costs as well as slower growth in discretionary spending partially offset by higher sales-related costs, primarily compensation, instrument amortization and sample expenses.

As a result of the adoption of the revised Statement No. 123, the Company's operating income for the first half of 2006 and 2005 were reduced by \$29.0 million and \$19.9 million, respectively, and the Company's net earnings for the same periods were reduced by \$18.8 million and \$12.9 million, respectively. Basic net earnings per share for the first half of 2006 and 2005 were reduced by \$.05 and \$.03, respectively and diluted net earnings per share were reduced by \$.05 and \$.03, respectively. The Company's operating income for the second quarter of 2006 and 2005 were reduced by \$14.2 million and \$10.1 million, respectively, and the Company's net earnings for the same periods were reduced by \$9.2 million and \$6.5 million, respectively. Basic and diluted net earnings per share for the second quarter of both 2006 and 2005 were reduced by \$.02.

Interest and investment income, which are included in other income (expense), increased to \$16.7 million in the first half of 2006 from \$3.4 million in 2005 as a result of increased cash and cash equivalents and marketable securities balances compared to the year earlier period.

The Company's effective income tax rates for the first half and second quarter of 2006 were 31.0% and 27.9%, respectively, as compared to effective income tax rates for the year ended December 31, 2005 and the first half and second quarter of 2005 of 32.6%, 29.3% and 29.2%, respectively. The effective income tax rate for the first half of 2006 reflects the impact of the non-deductibility for income tax purposes of the purchased in-process research and development charge associated with the acquisition of Sightline. The effective income tax rate, excluding the effect of the Sightline acquisition, for the first half of 2006 was reduced from 28.5% to 28.2% in the second quarter of 2006, thereby reducing income tax expense by \$1.8 million. The income tax rate reduction results primarily from increased manufacturing in lower tax jurisdictions and a favorable change in U.S. tax legislation enacted during the second quarter. The effective income tax rates for the 2005 periods have been restated to reflect the adoption of the revised Statement No. 123. The effective income tax rate for the year ended December 31, 2005 also reflects the non-deductibility for income tax purposes of the purchased in-process research and development charge associated with the acquisition of PlasmaSol Corp. as well as the third and fourth quarter 2005 income taxes associated with the repatriation of foreign earnings under the provisions of the American Jobs Creation Act.

Net earnings for the first half of 2006 were \$361.4 million, an increase of 5% compared to net earnings of \$344.5 million in the first half of 2005. Basic net earnings per share increased 5% in the first half of 2006 to \$.89 from \$.85 in 2005, and diluted net earnings per share increased 5% in the first half of 2006 to \$.88 from \$.84 in 2005. Net earnings for the second quarter of 2006 were \$213.9 million representing a 20% increase over net earnings of \$177.8 million in the second quarter of 2005. Basic net earnings per share increased 20% in the second quarter of 2006 to \$.53 from \$.44 in 2005, and diluted net earnings per share increased 21% in the second quarter of 2006 to \$.52 from \$.43 in 2005.

Excluding the impact of the \$52.7 million charge to write off purchased in-process research and development, adjusted net earnings for the first half of 2006 were \$414.1 million, representing a 20% increase over net earnings of \$344.5 million for the first half of 2005. Adjusted basic net earnings per share increased 20% in 2006 to \$1.02 from \$.85 and adjusted diluted net earnings per share increased 20% to \$1.01 from \$.84.

This adjusted financial measure does not replace the presentation of the Company's reported financial results stated under generally accepted accounting principles (GAAP). The Company has provided this supplemental non-GAAP financial measure because it provides meaningful information regarding the Company's results on a consistent and comparable basis for the periods presented. Management uses this non-GAAP financial measure for reviewing the operating results of its business segments and for analyzing potential future business trends in connection with its budget process. In addition, the Company believes investors will utilize this information to evaluate period-to-period results and to better understand potential future operating results. The Company encourages investors and other users of these financial statements to review its condensed consolidated financial statements and other publicly filed reports in their entirety and to not rely on any single financial measure.

The reconciliation of this non-GAAP financial measure is as follows (in millions):

| | Six Months Ended | | Percentage Change |
|--|------------------|----------------|----------------------|
| | 2006 | 2005 | |
| Reported net earnings | \$361.4 | \$344.5 | 5% |
| Purchased in-process research and development | 52.7 | -- | -- |
| Adjusted net earnings | <u>\$414.1</u> | <u>\$344.5</u> | 20 |
| Basic net earnings per share: | | | |
| Reported basic net earnings per share | \$.89 | \$.85 | 5 |
| Purchased in-process research and development | \$.13 | -- | -- |
| Adjusted basic net earnings per share | \$1.02 | \$.85 | 20 |
| Diluted net earnings per share: | | | |
| Reported diluted net earnings per share | \$.88 | \$.84 | 5 |
| Purchased in-process research and development | \$.13 | -- | -- |
| Adjusted diluted net earnings per share | \$1.01 | \$.84 | 20 |

Liquidity and Capital Resources

The Company's working capital at June 30, 2006, increased \$182.9 million to \$1,804.2 million from \$1,621.3 million at December 31, 2005. The increase in working capital resulted from growth in the Company's overall business and the use of cash earnings to fund increases in accounts receivable, inventories and prepaid expenses. Accounts receivable days sales outstanding increased 3 days to 57 days at June 30, 2006 from 54 days at December 31, 2005 and days sales in inventory increased 15 days to 129 days at June 30, 2006 from 114 days at December 31, 2005. The days sales outstanding at June 30, 2006 is consistent with historical levels. The increase in days sales in inventory is primarily due to increasing inventory balances in support of sales and anticipated product launches in the second half of the year.

The Company generated cash of \$216.5 million from operations in the first six months of 2006 compared to \$208.6 million in 2005. In the second quarter, the Company generated cash from operations of \$195.8 million compared to \$182.2 million in 2005. The increase in cash provided by operating activities in the first six months and second quarter of 2006 compared to 2005 is primarily due to increased earnings partially offset by changes in working capital accounts.

In the first half of 2006, the Company borrowed an additional \$84.8 million and used cash of \$311.6 million for payments on borrowings. The Company also used \$104.2 million for capital expenditures, \$79.3 million for acquisitions

and \$44.6 million for the payment of dividends; it also purchased and sold marketable securities. These securities are classified as available-for-sale investments in accordance with the provisions of FASB Statement No. 115, *Accounting for Certain Investments in Debt and Equity Securities*.

The Company had \$129.7 million in cash and cash equivalents and \$738.0 million in marketable securities at June 30, 2006. The Company had outstanding borrowings totaling \$14.2 million at the end of the first half of 2006. Current maturities of long-term debt at June 30, 2006 were \$13.5 million and are expected to decrease to \$7.6 million by December 31, 2006. The Company believes its cash on hand and marketable securities, as well as anticipated future cash flows from operations, will be sufficient to fund future operating capital requirements; future manufacturing facility construction and other capital expenditures; future business and product line acquisitions to supplement its current product offerings; loaner instrumentation for surgical implants in support of new product launches; and required debt repayments. Should additional funds be required, the Company had \$1,254.1 million of additional borrowing capacity available under all of its existing credit facilities, including the Company's \$1,000.0 million Unsecured Credit Facility. In addition, the Company had \$200.0 million of eligible accounts receivable that could be sold through its accounts receivable securitization facility at June 30, 2006.

Other Matters

The Company has certain investments in net assets in international locations that are not hedged. These investments are subject to translation gains and losses due to changes in foreign currencies. In the first half of 2006, the strengthening of foreign currencies relative to the U.S. dollar increased the value of these investments in net assets, and the related deferred gain in shareholders' equity, by \$50.7 million.

In December 2003, the Company announced that its subsidiary Physiotherapy Associates, Inc., and Stryker received a subpoena from the United States Attorney's Office in Boston, Massachusetts, in connection with a Department of Justice investigation of Physiotherapy Associates' billing and coding practices. In March 2005, the Company announced that it received a subpoena from the United States Department of Justice requesting documents for the period January 2002 through the present relating to "any and all consulting contracts, professional service agreements, or remuneration agreements between Stryker Corporation and any orthopedic surgeon, orthopedic surgeon in training, or medical school graduate using or considering the surgical use of hip or knee joint replacement/reconstruction products manufactured or sold by Stryker Corporation." In June 2006, the Company announced that it received a subpoena from the United States Department of Justice, Antitrust Division requesting documents for the period January 2001 through the present regarding possible violations of federal criminal law, including possible violation of the antitrust laws, relating to the manufacture and sale of orthopaedic implant devices. The Company is fully cooperating with the Department of Justice regarding these matters.

In June 2006, the FASB issued Interpretation No. 48, *Accounting for Uncertainty in Income Taxes, an Interpretation of FASB Statement No. 109*. This Interpretation clarifies the accounting for income taxes by prescribing the minimum recognition threshold a tax position is required to meet before being recognized in the financial statements. The Interpretation also provides guidance for the measurement and classification of tax positions, interest and penalties, and requires additional disclosure on an annual basis. The Company plans to adopt the provisions of the Interpretation effective January 1, 2007, as required. The Company has not yet determined what effect the adoption of the Interpretation will have on net earnings, net earnings per share and the financial position of the Company, however, any difference between the amounts recognized in the Company's financial statements prior to the adoption of the Interpretation and the amounts reported after the adoption will be accounted for as a cumulative-effect adjustment recorded in the beginning balance of retained earnings and will not require restatement of prior periods.

In the second quarter of 2006, the Company announced that it submitted a pre-market approval (PMA) application to the United States Food and Drug Administration (FDA) for the use of OP-1 Putty for posterolateral lumbar spine fusion surgeries. The product, OP-1 Putty, which contains the recombinant human protein OP-1 that stimulates new bone formation, is currently approved in the United States under a humanitarian device exemption (HDE) for a specific revision spine indication. The HDE approval limits the use of the product in the United States to a patient population of 4,000 per year. A related product, OP-1 Implant for nonunion bone fractures, is approved in 28 countries, including an HDE approval in the United States.

Forward-Looking Statements

This report contains information that includes or is based on forward-looking statements within the meaning of the federal securities law that are subject to various risks and uncertainties that could cause the Company's actual results to differ materially from those expressed or implied in such statements. Such factors include, but are not limited to: pricing pressures generally, including cost-containment measures that could adversely affect the price of or demand for the Company's products; regulatory actions; unanticipated issues arising in connection with clinical studies and eventual United States Food and Drug Administration approval of additional OP-1 applications, the FlexiCore and CerviCore spinal implant products, the PlasmaSol sterilization products or other new product introductions; integration and other issues that could delay the introduction of the recently acquired Sightline product line; 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.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISKS

There have been no material changes from the information provided in the Company's Annual Report on Form 10-K for the year ended December 31, 2005.

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures – An evaluation of the effectiveness of the design and operation of the Company's disclosure controls and procedures as of June 30, 2006 was carried out under the supervision and with the participation of the Company's management, including the President and Chief Executive Officer and the Vice President and Chief Financial Officer ("the Certifying Officers"). Based on that evaluation, the Certifying Officers concluded that the Company's disclosure controls and procedures are effective to bring to the attention of the Company's management the relevant information necessary to permit an assessment of the need to disclose material developments and risks pertaining to the Company's business in its periodic filings with the Securities and Exchange Commission. There was no change to the Company's internal control over financial reporting during the quarter ended June 30, 2006 that materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

Other Matters – The Company has begun the process of implementing new Enterprise Resource Planning (ERP) systems at certain of its divisions. An ERP system is a fully-integrated set of programs and databases that incorporate order processing, production planning and scheduling, purchasing, accounts receivable and inventory management and accounting. During the first quarter of 2006, the Company's domestic locations of its Orthopaedics and Spine divisions transitioned to their new ERP systems. The Company's Endoscopy division began to transition to its new ERP system in July of 2006. In connection with these ERP system implementations, the Company has and will update its internal controls over financial reporting, as necessary, to accommodate modifications to its business processes and accounting procedures. The Company does not believe that these ERP system implementations have had or will have an adverse effect on the Company's internal control over financial reporting.

PART II. – OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

There have been no material changes from the information provided in the Company's Annual Report on Form 10-K for the year ended December 31, 2005.

ITEM 1A. RISK FACTORS

There have been no material changes from the information provided in the Company's Annual Report on Form 10-K for the year ended December 31, 2005.

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

- (c) The Company issued 2,552 shares of Common Stock in the second quarter of 2006 as performance incentive awards to certain employees. These shares were not registered under the Securities Act of 1933 based on the conclusion that the awards would not be events of sale within the meaning of Section 2(a)(3) of the Act.

ITEM 6. EXHIBITS

(a) Exhibits

31(i) Certification of Principal Executive Officer of Stryker Corporation pursuant to Rule 13a-14(a)

31(ii) Certification of Principal Financial Officer of Stryker Corporation pursuant to Rule 13a-14(a)

32(i) Certification by Chief Executive Officer of Stryker Corporation pursuant to 18 U.S.C. Section 1350

32(ii) Certification by Chief Financial Officer of Stryker Corporation pursuant to 18 U.S.C. Section 1350

SIGNATURES

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

STRYKER CORPORATION
(Registrant)

August 9, 2006
Date

/s/ STEPHEN P. MACMILLAN
Stephen P. MacMillan, President
and Chief Executive Officer
(Principal Executive Officer)

August 9, 2006
Date

/s/ DEAN H. BERGY
Dean H. Bergy, Vice President
and Chief Financial Officer
(Principal Financial Officer)

EXHIBIT INDEX

Exhibit 31 - Rule 13a-14(a) Certifications

- (i) Certification of Principal Executive Officer of Stryker Corporation
- (ii) Certification of Principal Financial Officer of Stryker Corporation

Exhibit 32 - 18 U.S.C. Section 1350 Certifications

- (i) Certification by Chief Executive Officer of Stryker Corporation
- (ii) Certification by Chief Financial Officer of Stryker Corporation

CERTIFICATION OF PRINCIPAL EXECUTIVE OFFICER

I, Stephen P. MacMillan, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q for the quarter ended June 30, 2006 of Stryker Corporation;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors:
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: August 9, 2006

/s/ STEPHEN P. MACMILLAN
Stephen P. MacMillan
President and Chief Executive Officer

CERTIFICATION OF PRINCIPAL FINANCIAL OFFICER

I, Dean H. Bergy, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q for the quarter ended June 30, 2006 of Stryker Corporation;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent functions):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: August 9, 2006

/s/ DEAN H. BERGY

Dean H. Bergy

Vice President and Chief Financial Officer

**CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report on Form 10-Q of Stryker Corporation (the "Company") for the quarter ending June 30, 2006 (the "Report"), I, Stephen P. MacMillan, Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

- (1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ STEPHEN P. MACMILLAN
Stephen P. MacMillan,
Chief Executive Officer

August 9, 2006

**CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report on Form 10-Q of Stryker Corporation (the “Company”) for the quarter ending June 30, 2006 (the “Report”), I, Dean H. Bergy, Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

- (1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition results of operations of the Company.

/s/ DEAN H. BERGY
Dean H. Bergy
Chief Financial Officer

August 9, 2006