Intuitive Surgical

David Gardner | November 19, 2008

CURRENT PRICE: ISRG $ 555.11 ↑ $ 0.15 (0.0%)

Why Buy:

- Disruptive technology is still early in its adoption cycle and continues to expand into new procedures.
- Recurring training and instruments now make up nearly half of revenue.
- The stock's decline gives us another great opportunity to buy a Core Rule Breaker that's succeeded time and time again.

What It Does

Intuitive Surgical's noninvasive da Vinci robot is revolutionizing surgery.

Key Company Data

Headquarters: Sunnyvale, Calif.

Website: www.intuitivesurgical.com

CAPS Rating: 4 Stars (72.30 out of 100)

Sign of a Breaker: True Rule Breaker

Market Cap: $5,805

Cash / Debt: $408.2 / $0

Revenue (TTM): $832.8

Earnings (TTM): $202.7

Revenue (2005-07): $227.3 / $372.7 / $600.8

Earnings (2005-07): $94.1 / $72.0 / $144.5

Recent Price: $148.41

Data as of 11/14/08
Dollar amounts in millions except recent price.

Our Innovation Tour took us in search of groundbreaking companies with great potential. We kicked off our trip by talking with the top brass at **Intuitive Surgical** (NASDAQ: ISRG), and with their words in mind as I scan the growth-stock universe, it's clear that this quintessential Rule Breaker is one to buy again.

"This is not about this quarter or next," CEO Lonnie Smith told us. "This is about changing surgery." That's the ultimate Rule Breaking attitude, and it's made Intuitive a favorite in our service. I believe every member should own shares of this Core Rule Breaker, and now is a great time to buy into this long-term leader that's out to change the world.

Domo Arigato, Mr. Roboto

Intuitive's da Vinci robot is the precise extension of a surgeon's hands and tools. These remote operations offer the advantages of smaller incisions and superior outcomes. Most hospitals believe the da Vinci saves them money by lowering complication rates and hospital stays, while also attracting patients with the prospect of faster recoveries.

The da Vinci made its mark in prostatectomies, and those still account for most procedures. But the fastest-growing applications are now in gynecology, particularly hysterectomies. Management stresses that the da Vinci is a disruptive technology *still early in its adoption cycle*.

Analysts once worried about when the da Vinci would reach saturation in urology, but that hasn't happened. As doctors get used to it for prostatectomies, they've naturally started using it for other procedures. There's been the same expansion in gynecology, while cardiology, gastrology, and other areas remain largely unexploited. Far from saturation, there are many more systems to sell, in the U.S. and abroad.

Getting Better With Age

Intuitive was a steal when we first recommended it at $44 in 2005, but the stock's recent fall leaves lots of room to profit from the company's great growth trajectory:

Scroll left/right to view wide tables

	2004	**2005**	**2006**	**2007**	**TTM**
Year-End Price	$40.02	$117.27	$95.90	$323.00	$148.41
Earnings Per Share	$0.67	$2.51*	$1.89	$3.70	$5.08
Year-Over-Year Revenue Growth	51%	64%	64%	61%	59%
Trailing P/E	60	47	51	87	29
EV to Operating Cash Flow	41	59	33	58	21

**Earnings in 2005 were boosted by a large one-time tax benefit. At a normalized rate, the P/E would have been about 95. Trailing 12 months through 9/30/08; stock price through 11/14/08.*

Intuitive has managed remarkably strong, stable growth. Revenue increased at a faster pace in the past 12 months than it did in the year leading up to our first recommendation, and it's still only slightly below its peak growth rate. Yet the stock trades at its lowest multiple to cash flow and its lowest P/E since 2004. Revenue is less at risk now because the large installed base means more recurring sales. Training, instruments, and accessories now account for 46% of sales.

"This is a disruptive technology that will be adopted over a long period of time," Smith said. "If you're in it for the long term, then we would love to have you as an investor." We've loved being investors, and we think you will, too.

Read our full interview with Intuitive, then join us on the RBS: Intuitive Surgical discussion board.

David owns shares of Intuitive Surgical.