Philips Lighting reports second quarter sales of EUR 1.7 billion and operational profitability of 10.2%

Q2 2017 results
Analyst & Investor presentation

July 21, 2017
Agenda

Business and operational performance by Eric Rondolat

Financial performance by Stéphane Rougeot

Outlook and conclusion by Eric Rondolat

Q&A
Philips Lighting reports second quarter sales of EUR 1.7 billion and operational profitability of 10.2%

Key observations for Q2 2017

- Comparable sales declined by 1.8%
- Total LED-based sales increased by 14%
- Europe delivered robust growth
- The Americas and the Middle East & Turkey, most notably Saudi Arabia, remain impacted by softer market conditions

- Adjusted EBITA margin increased to 10.2%; or 9.4% excl. EUR 15m real estate gain in Home
- Net income: EUR 73m
- Free cash flow: EUR -27m, reflecting an increase in inventories to support anticipated growth in H2 2017
Each business group increased its Adjusted EBITA margin

<table>
<thead>
<tr>
<th>Q2 2017</th>
<th>CSG %</th>
<th>Adjusted EBITA (€m)</th>
<th>vs LY (€m)</th>
<th>Adjusted EBITA %</th>
<th>vs LY (bps)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Lamps</td>
<td>-18.2%</td>
<td>95</td>
<td>-22</td>
<td>20.7%</td>
<td>+20</td>
</tr>
<tr>
<td>LED</td>
<td>20.9%</td>
<td>45</td>
<td>16</td>
<td>10.6%</td>
<td>+220</td>
</tr>
<tr>
<td>Professional</td>
<td>-2.7%</td>
<td>48</td>
<td>2</td>
<td>7.2%</td>
<td>+50</td>
</tr>
<tr>
<td>Home</td>
<td>15.5%</td>
<td>12</td>
<td>22</td>
<td>8.2%</td>
<td>+1,610</td>
</tr>
<tr>
<td>Philips Lighting</td>
<td>-1.8%</td>
<td>174</td>
<td>13</td>
<td>10.2%</td>
<td>+90</td>
</tr>
</tbody>
</table>
Increasing profitability at LED, Professional and Home more than offsets decreasing profit contribution of Lamps

<table>
<thead>
<tr>
<th>Segment</th>
<th>Adjusted EBITA Q2 16 margin</th>
<th>Lamps</th>
<th>LED</th>
<th>Professional</th>
<th>Home</th>
<th>Other</th>
<th>Adjusted EBITA Q2 17 margin</th>
</tr>
</thead>
<tbody>
<tr>
<td>Home</td>
<td>9.3%</td>
<td>-70 bps</td>
<td>50 bps</td>
<td>20 bps</td>
<td></td>
<td>30 bps</td>
<td>-20 bps</td>
</tr>
<tr>
<td>Other</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>110 bps</td>
</tr>
<tr>
<td>LED</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>80 bps</td>
</tr>
<tr>
<td>Professional</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>9.4%</td>
</tr>
</tbody>
</table>

Contribution of the EUR 15m real estate gain in Home
Lamps improved profitability, driven by manufacturing footprint optimization

Key observations for Q2 2017

- Comparable sales declined by 18.2%
- In H1 2017, we estimate that the conventional lighting market declined at a faster pace than our Lamps business, which has resulted in continued market share gains

- Adjusted EBITA margin increased by 20 bps to 20.7%
LED volumes grew significantly and margin continued to improve

Key observations for Q2 2017

- CSG of 20.9% driven by significant volume growth, partly offset by lower selling prices and stronger growth in affordable products
- Continue to see positive impact of measures implemented last year
- All regions contributed to growth; countries with low LED penetration rates showed higher growth

- Adjusted EBITA margin improved by 220 bps, driven by:
  - Operational leverage
  - Procurement savings
  - Offsetting price reductions and mix impact
Professional improved profitability despite soft market conditions in some key markets

Key observations for Q2 2017

- Europe and Greater China remained strong
- Market conditions in the US continued to be soft, particularly for small- to medium-sized projects
- Order backlog for larger projects in the US continues to be strong and is expected to positively impact CSG and the Adjusted EBITA margin in H2 2017
- Market conditions in Saudi Arabia continued to be challenging, negatively impacting CSG by 180 bps

- Adjusted EBITA margin increased by 50 bps to 7.2%, driven by:
  - Procurement savings
  - Mix improvement

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1 KSA: Kingdom of Saudi Arabia
Home delivered double-digit growth and is on track to become profitable for FY 2017

**Key observations for Q2 2017**

- Comparable sales growth of 15.5%:
  - Driven by both Home Systems and Home Luminaires
  - All regions contributed to growth
- To support the growth of the Philips Hue offering, investments were stepped-up in:
  - Innovation
  - Marketing
  - Supply chain

- Adjusted EBITA margin increased from -7.9% to 8.2%. Excluding the gain on real estate of EUR 15m, Adjusted EBITA margin improved to -2.1%, driven by:
  - Operational leverage
  - Procurement savings
  Partly offset by increased investments in Philips Hue

<table>
<thead>
<tr>
<th>Sales (in EURm) &amp; comparable sales growth (in %)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2Q16</td>
</tr>
<tr>
<td>14.3%</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Adjusted EBITA (in EURm &amp; as % of sales)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2Q16</td>
</tr>
<tr>
<td>-10</td>
</tr>
<tr>
<td>-7.9%</td>
</tr>
</tbody>
</table>
H1 2017 performance: on track to deliver on outlook for the year

Progress in H1 2017

- Improved comparable sales trend

Adjusted EBITA margin improved to 9.4% (8.9% excl. real estate gain in Q2 2017)

Free cash flow

- FCF was EUR -26m, reflecting an increase in inventories to support growth in H2
LED-based sales grew by 17% to EUR 2.1bn in H1 2017

Development of LED-based sales (in % of total sales)

LED-based sales H1 2017: EUR 2.1bn, CSG 17%
Agenda

Business and operational performance by Eric Rondolat

Financial performance by Stéphane Rougeot

Outlook and conclusion by Eric Rondolat

Q&A
Adjusted EBITA margin improvement in Q2 2017 primarily driven by procurement and productivity savings

Adjusted EBITA (in EURm)

as % of sales

2Q16 | Volume / Mix | Price | CoGS | Indirect Costs | Currency | Other business income* | 2Q17

9.3% | (35) | (100) | 111 | 9 | 12 | 16 | 174

+90 bps

Gross margin + 30 bps

*) Other business income includes a real estate gain in Home of EUR 15m
Developments in adjusted indirect costs in Q2 2017

**Key observations for Q2 2017**

- Negative currency impact of EUR 3m
- Indirect cost reduction of EUR 9m, including additional investments to support growth
- Executing a detailed plan to realize cost savings:
  - Selling expenses
  - IT
  - Real Estate
  - Finance
  - HR

### Adjusted indirect costs

<table>
<thead>
<tr>
<th>Category</th>
<th>Adjusted indirect costs 2Q16</th>
<th>Currency impact</th>
<th>Indirect cost savings</th>
<th>Adjusted indirect costs 2Q17</th>
</tr>
</thead>
<tbody>
<tr>
<td>Adj. R&amp;D</td>
<td>473</td>
<td>-82</td>
<td>3</td>
<td>466</td>
</tr>
<tr>
<td>Adj. SG&amp;A</td>
<td>555</td>
<td>3</td>
<td>-9</td>
<td>549</td>
</tr>
</tbody>
</table>

As % of sales 32.0% → +30 bps → 32.3%
Working capital as % of sales improved by 130 basis points y-o-y to 10.9% despite an increase in inventories to support sales growth in H2 2017.

**Working capital**¹ (in EURm & as % of sales)

<table>
<thead>
<tr>
<th></th>
<th>3Q15</th>
<th>4Q15</th>
<th>1Q16</th>
<th>2Q17</th>
</tr>
</thead>
<tbody>
<tr>
<td>%</td>
<td>14.1%</td>
<td>11.1%</td>
<td>11.6%</td>
<td>12.2%</td>
</tr>
<tr>
<td>Value</td>
<td>1,047</td>
<td>832</td>
<td>865</td>
<td>895</td>
</tr>
</tbody>
</table>

**Inventories** (in EURm & as % of sales)

<table>
<thead>
<tr>
<th></th>
<th>3Q15</th>
<th>4Q15</th>
<th>1Q16</th>
<th>2Q17</th>
</tr>
</thead>
<tbody>
<tr>
<td>%</td>
<td>15.7%</td>
<td>13.2%</td>
<td>13.6%</td>
<td>14.1%</td>
</tr>
<tr>
<td>Value</td>
<td>1,162</td>
<td>988</td>
<td>1,010</td>
<td>1,030</td>
</tr>
</tbody>
</table>

¹ Working capital includes inventories, receivables, accounts and notes payable, other current assets & liabilities, derivative financial assets & liabilities, income tax receivable & payable, and accrued liabilities.
Net debt increase of EUR 281m due to dividend payment and share buy-back

In EURm

- Net debt end 1Q17: 416
- EBITDA: 176
- Change in working capital: 136
- Net capex: 10
- Change in provisions: 11
- Interest & Tax: 31
- Other FCF items*: 15
- Dividend: 121
- Share buy-back: 24
- Other: 697
- Net debt end 2Q17: 697

*) This includes the gain on the sale of real estate
Capital allocation policy

**Cash available**

- Continued free cash flow generation
- Managing our financial ratios to maintain a financing structure compatible with an investment-grade profile

**Cash uses**

- Annual regular cash dividend within 40-50% of continuing net income*; dividend paid of EUR 157m
- Disciplined management of balance sheet liabilities, including an active pension de-risking strategy
  - Intend to contribute approx. USD 150m to our US pension fund over the period 2017-2019, to further reduce the liabilities and to lower interest expenses going forward
  - First contribution of USD 50m is planned for Q3 2017
- Returning up to EUR 300m to our shareholders in the period 2017-2018 by participating in share disposals by our main shareholder (EUR 183m to date)
- Seizing non-organic opportunities primarily through small- to medium-sized acquisitions

*Continuing net income: recurring net income from continuing operations, or net income excluding discontinued operations and excluding material non-recurring items such as restructuring, acquisition-related and separation charges
Agenda

Business and operational performance by Eric Rondolat

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Q&A
On track to deliver our 2017 outlook

• Further improvement of Adjusted EBITA margin: approximately 50-100 basis points in 2017, excluding a real estate gain of EUR 15m in Q2 2017

• Deliver solid free cash flow

• Confident that we will return to positive comparable sales growth in the course of this year
Currency movements had a positive impact on both sales and Adjusted EBITA

Key observations

- Currency movements had a positive impact on both sales and Adjusted EBITA in the second quarter
  - Sales impact from currencies of EUR 21m, mainly from the US dollar
  - Adjusted EBITA impact of EUR 12m, mainly from the CNY and US dollar
- Philips Lighting policy is to hedge 100% of committed FX transactions and anticipated transactions up to 80% in layers over the next 15 months
Net income of EUR 73m driven by higher operating profit and lower financial expenses

<table>
<thead>
<tr>
<th>From Adjusted EBITA to net income (in EURm)</th>
<th>2Q16</th>
<th>2Q17</th>
</tr>
</thead>
<tbody>
<tr>
<td>Adjusted EBITA</td>
<td>161</td>
<td>174</td>
</tr>
<tr>
<td>- Restructuring</td>
<td>-23</td>
<td>-30</td>
</tr>
<tr>
<td>- Acquisition related charges</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>- Other incidental items</td>
<td>-15</td>
<td>-5</td>
</tr>
<tr>
<td>EBIT</td>
<td>123</td>
<td>139</td>
</tr>
<tr>
<td>- Amortization</td>
<td>-27</td>
<td>-28</td>
</tr>
<tr>
<td>EBIT</td>
<td>96</td>
<td>111</td>
</tr>
<tr>
<td>Net financial income / expenses</td>
<td>-26</td>
<td>-11</td>
</tr>
<tr>
<td>Income tax expense</td>
<td>-14</td>
<td>-26</td>
</tr>
<tr>
<td>Results relating to investments in</td>
<td>1</td>
<td>-1</td>
</tr>
<tr>
<td><strong>Net income</strong></td>
<td><strong>57</strong></td>
<td><strong>73</strong></td>
</tr>
</tbody>
</table>

**Key observations**

1. Separation costs of EUR 5m in Q2 2017

2. Financial expenses in Q2 2016 reflect higher interest rates paid on loans with Royal Philips

3. Income tax expense increased by EUR 12m largely due to higher taxable earnings
Free Cash Flow of EUR -27m

### Free cash flow (in EURm)

<table>
<thead>
<tr>
<th></th>
<th>2Q16</th>
<th>2Q17</th>
</tr>
</thead>
<tbody>
<tr>
<td>Income from operations</td>
<td>96</td>
<td>111</td>
</tr>
<tr>
<td>Depreciation and amortization</td>
<td>68</td>
<td>65</td>
</tr>
<tr>
<td>Change in working capital</td>
<td>-36</td>
<td>-136</td>
</tr>
<tr>
<td>Net capex</td>
<td>-22</td>
<td>-10</td>
</tr>
<tr>
<td>Change in provisions</td>
<td>-27</td>
<td>-11</td>
</tr>
<tr>
<td>Interest paid</td>
<td>-6</td>
<td>-4</td>
</tr>
<tr>
<td>Income taxes paid</td>
<td>-20</td>
<td>-27</td>
</tr>
<tr>
<td>Other</td>
<td>7</td>
<td>-15</td>
</tr>
<tr>
<td><strong>Free cash flow</strong></td>
<td><strong>60</strong></td>
<td><strong>-27</strong></td>
</tr>
<tr>
<td><strong>As % of sales</strong></td>
<td><strong>3.5%</strong></td>
<td><strong>-1.6%</strong></td>
</tr>
</tbody>
</table>

### Key observations

- Free cash flow decline of EUR 87m:
  - Higher cash outflow on working capital
  - Higher tax income paid
- Cash outflow restructuring EUR 22m and separation EUR 10m
## Real estate gains in the first half of 2017

<table>
<thead>
<tr>
<th></th>
<th>Q1 2017</th>
<th>Q2 2017</th>
<th>H1 2017</th>
</tr>
</thead>
<tbody>
<tr>
<td>Lamps</td>
<td>10</td>
<td>0</td>
<td>10</td>
</tr>
<tr>
<td>LED</td>
<td>3</td>
<td>0</td>
<td>3</td>
</tr>
<tr>
<td>Professional</td>
<td>3</td>
<td>0</td>
<td>3</td>
</tr>
<tr>
<td>Home</td>
<td>0</td>
<td>15</td>
<td>15</td>
</tr>
<tr>
<td><strong>Philips Lighting</strong></td>
<td><strong>16</strong></td>
<td><strong>15</strong></td>
<td><strong>31</strong></td>
</tr>
</tbody>
</table>
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