

Annual Report 2020

Message from the CEO

“Faced with the COVID-19 pandemic, Philips demonstrated strength and agility, working intensely together with healthcare providers to cope with the challenges for both acute and regular healthcare. At the same time we continued to support people with their personal health. More than ever, we have the potential to accelerate the transformation of healthcare with our innovative solutions.”

Frans van Houten CEO Royal Philips

Dear Stakeholder,

In 2020, Philips again demonstrated its relevance in bringing meaningful innovation to improve people's health and well-being, as we responded to the COVID-19 pandemic. As a company, we continue to focus on delivering against our triple duty of care – meeting critical customer needs, safeguarding the health and safety of our employees, and ensuring business continuity.

Our employees displayed flexibility and resourcefulness as we more than quadrupled output of acute care equipment and solutions to help frontline healthcare workers diagnose, treat, monitor and manage COVID-19 patients. We significantly increased production of critical care ventilators, provided ICU monitoring & analytics solutions, and rolled out telehealth solutions to relieve the pressure on scarce resources. And our field service engineers worked round the clock to support healthcare providers in their hour of need.

In parallel, we continued to support health systems with the delivery of regular care, entering into multiple long-term strategic partnerships – all featuring result-oriented business models – to transform healthcare by enhancing patient care and improving productivity. We also found new ways to serve consumers seeking to live a healthy life, prevent disease and proactively manage their own health. In total, our products and solutions improved the lives of 1.75 billion people in 2020, including 207 million people in underserved communities.

Overall, our company performance proved resilient. While some of our businesses were affected by lower demand, others were able to significantly increase deliveries. I would like to express my admiration and gratitude for the way in which the extended Philips family – our employees, our suppliers and partners, the Philips Foundation – pulled together with our customers to address the impact of the pandemic.

Affirmation of our strategy

The developments of the past year validate our strategy to innovate the provision of care along the health continuum – putting the patient at the center, improving diagnosis and treatment pathways, enabling the integration of care across care settings, and increasing care provider productivity. At the same time, we help consumers to live healthier lifestyles and to cope with chronic disease. Increasingly, we are able to connect home and hospital care through telehealth platforms. This approach is resonating more strongly than ever.

Customers appreciate the comprehensive and strategic view we take of the future of health and healthcare. They want innovative solutions – smart combinations of systems, devices, informatics, data and services – that can help them deliver on the Quadruple Aim of better health outcomes, improved patient experience, improved staff experience, and lower cost of care. Given the learnings from COVID-19, they are especially keen to discover how we can support care outside the hospital.

In recent years, we have invested significantly in data science, informatics and cloud technology to enable the delivery of integrated solutions across the health continuum, and across care settings. These investments are now paying off, with a rapid increase in adoption of, for example, e-ICU and telehealth solutions that facilitate collaboration between health professionals and patient engagement.

Designed to address customer needs, our health technology innovations – supporting personal health, precision diagnosis, image-guided therapies and connected care, and leveraging the power of data and informatics – continue to generate a growing proportion of solutions-based sales and recurring revenues, which now stand at around 37% of total sales.

Innovating to address global health challenges

In healthcare the world over, we are seeing an increased focus on productivity and outcome-based models, as well as care outside the hospital. COVID-19 has accelerated the digitalization of care and the adoption of telehealth. This shift is being reinforced by global trends such as aging populations, the rise of chronic diseases, and resource constraints.

Innovative health technology can help health systems address these challenges, as well as extend access to care to those in need. The HealthTech market is a very attractive and sizable one, with considerable growth and margin potential, and Philips already holds strong leadership positions in over 65% of our portfolio.

Inspired by our purpose to improve people's health and well-being, we invest almost 10% of revenue in Research & Development to innovate solutions that make a difference

to our customers and society at large. Helping people to stay healthy and prevent disease, for instance through our expanding teledentistry services. Giving clinicians AI-assisted tools like our new Radiology Workflow Suite that help them make precision diagnoses and select the best care pathway. Helping surgeons deliver personalized, minimally invasive treatment with solutions like our constantly evolving Azurion image-guided therapy platform. And outside the hospital – orchestrating and delivering care in lower-cost care settings, helping people to recover, or live with chronic disease, at home.

All of these require a seamless flow of data, which is enabled by our highly secure connected care solutions, such as our IntelliVue MX750/MX850 patient monitors for the ICU. To unlock the full benefits of data-enabled care, we continue to expand our capabilities in informatics and data science, with around half of our R&D professionals working in these areas.

Doing business responsibly and sustainably

In 2020, we underscored our determination to lead by example by renewing our purpose – to improve people's health and well-being through meaningful innovation, with the aim of improving 2 billion lives per year by 2025, including 300 million in underserved communities, rising to 2.5 billion and 400 million respectively by 2030.

This is part of an enhanced, fully integrated approach to doing business responsibly and sustainably. Building on our strong heritage in environmental and social responsibility, this new framework comprises a comprehensive set of key commitments across the Environmental, Social and Governance (ESG) dimensions that guide our endeavors. I am convinced this is the best way for Philips to create superior, long-term value for our many stakeholders.

I am pleased that we have delivered on all the targets set out in our Healthy people, Sustainable planet 2016–2020 program. As a purpose-driven company, we are conscious of our responsibility towards society and of the need to continue to embed sustainability ever deeper in the way we do business. Having become carbon-neutral in our own operations in 2020, we are now extending our ambitions and working with our partners to ensure that emissions across our entire value chain are in line to limit global warming to the 1.5 °C scenario.

We received further recognition for our efforts in this area in 2020 – achieving a CDP 'A List' rating for the eighth consecutive year for our action on climate change, and securing the second-highest place in both the global Dow Jones Sustainability Indices (DJSI) list and The Wall Street Journal's new ranking, 100 Most Sustainably Managed Companies in the World.

Our performance in 2020

COVID-19 impacted every part of our business in 2020. Nevertheless, despite the challenging circumstances, we were able to execute our plans and return to growth in the second half of the year. For the full year we delivered 3% comparable sales growth*) and a strong free cash flow**) of EUR 1.9 billion. Comparable order intake**) increased 9% and we made market share gains in a number of our health systems businesses.

Our Diagnosis & Treatment businesses were impacted by the ongoing postponement of capital equipment installations and routine care, including elective procedures, yet continued to deliver a steady flow of innovations designed to help clinicians deliver a precision diagnosis leading to targeted therapies.

Our Connected Care businesses posted exceptional growth, fueled by COVID-19-related demand for our hospital ventilation and monitoring & analytics solutions.

Our Personal Health businesses had to contend with a steep decrease in consumer demand brought about by the onset of COVID-19, yet rebounded strongly by accelerating online growth, increasing digital engagement, entering into partnerships with leading retailers, and scaling direct-to-consumer business models.

We initiated the process to create a separate legal structure for our Domestic Appliances business within the Philips Group, and we expect to complete this process by Q3 2021.

We made several acquisitions in 2020. For instance, we expanded our image-guided therapy devices portfolio, acquiring Intact Vascular to add an industry-first implantable device to treat peripheral artery disease. We also agreed to acquire BioTelemetry (completed on February 9, 2021) and Capsule Technologies to strengthen our Connected Care segment. These acquisitions will further broaden and scale our patient care management solutions for the hospital and the home, enhance patient outcomes, streamline clinical workflows and increase productivity.

Looking ahead, we continue to see uncertainty related to the impact of COVID-19 across the world. For 2021, Philips plans to deliver low-single-digit comparable sales growth*), driven by solid growth in Diagnosis & Treatment and Personal Health, partly offset by lower Connected Care sales, and an Adjusted EBITA margin*) improvement of 60-80 basis points.

Reflecting our confidence in the future course of the company and the importance we attach to dividend stability, we propose to maintain the dividend at EUR 0.85 per share.

*) Non-IFRS financial measure. For the definition and reconciliation of the most directly comparable IFRS measure, refer to Reconciliation of non-IFRS information.

**) Other Key Performance Indicator. For the definition and further information, refer to Other Key Performance Indicators.

Transforming to create greater value

As we continue our transformation into a customer-first solutions company, we are guided by our strategic roadmap, with its three key imperatives:

- Further improving the customer experience and operational excellence
- Boosting growth in the core by innovating to extend category leadership, geographic expansion, and deeper customer partnerships
- Winning with solutions to support consumers with their personal health, and to help professional healthcare customers achieve the Quadruple Aim.

We aim to drive customer preference by getting even closer to our customers and consumers, making Philips easier to do business with, and further improving our quality, operational excellence and productivity. To do this, we are driving the digital transformation in every area of our business, leveraging our integrated IT landscape – from the way we connect and engage with our customers and consumers to seamlessly connecting our solutions, e.g. to enable remote servicing and upgrades.

In our core business we aim to drive growth through innovation by capturing geographic growth opportunities and by continuing the pivot to consultative customer partnerships and business models, which offer a deeper relationship, with recurring revenue streams.

We will also continue the shift towards integrated solutions with demonstrable clinical evidence and health economic benefits that help our customers achieve the Quadruple Aim. In doing so, we will leverage data science and AI at scale. Where appropriate, we will continue to make acquisitions and enter into partnerships to support our organic growth.

By working in accordance with the Philips Business System and executing on these imperatives with urgency and discipline, we will be able to create more value for our stakeholders – driving customer preference, sustained growth, margin expansion, increased cash flow and improved return on invested capital, while delivering on our ESG commitments.

In conclusion

Once again, I would like to thank our customers, suppliers and partners for working together with Philips in the fight against coronavirus. I also want to express my gratitude to our employees for their commitment, resourcefulness and hard work in difficult circumstances. And I wish to thank our shareholders for the confidence they continue to show in Philips.

Our strategic focus and commitment to improvement remain undiminished. Energized by our purpose and buoyed by the resilience and agility I have seen over the past year, I am confident in Philips' ability to maintain our transformation momentum, truly impact global health challenges through innovation, and deliver sustained value for our many, diverse stakeholders.

Frans van Houten, Chief Executive Officer

