

Annual Report 2022

Message from the CEO

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“2022 was a very disappointing year for Philips and its stakeholders, and we are taking firm action to strengthen patient safety and quality, improve our execution and step up performance with urgency in 2023.”

Roy Jakobs CEO Royal Philips

Dear Stakeholder,

Philips is a company with strong market leadership positions, an extensive customer base, strong innovation portfolio, talented employees, and a global purpose-driven brand. Yet, as our 2022 performance underlines, we are not extracting the full value of our businesses and have disappointed many stakeholders.

My priority as CEO is to address operational challenges, improve performance, and drive progressive value creation through a strategy of focused organic growth and an innovation model shift to increase the impact of patient- and people-centric innovation at scale. Execution will be the key value driver, with three clear priorities around improving patient safety and quality, creating more reliable and resilient supply chains, and simplifying the way we work, so we are more agile and competitive.

Addressing priority challenges – improved execution as key value driver

Our first priority is to rebuild Philips’ reputation around patient safety and quality. The recall of specific Respiroics sleep therapy devices and ventilators let down the patients who depended on them, and the doctors caring for those patients. We apologize deeply for that and are working hard to restore trust with all stakeholders. By year-end, following the substantial ramp-up of capacity, Philips Respiroics had completed around 90% of the production required for the delivery of replacement devices to patients.

In consultation with regulators around the world, we have also been conducting a comprehensive test and research program to better understand the potential health risks associated with the use of affected devices. I am very conscious that 18 months is long, but this work had to be done thoroughly. I am encouraged by the test results for the first-generation DreamStation devices, that account for over two thirds of the registered affected devices: the prevalence of visible foam degradation is low, and the emission of the detected volatile organic compounds and particulates are within the applicable safety limits and not expected to result in appreciable harm to health in patients.

We are fully committed to completing the Respiroics recall and testing program in 2023.

We will also implement all measures agreed with the US Food & Drug Administration (FDA) and US Department of Justice, including a consent decree, and rebuild ties with the FDA and other national regulators. We have put the leadership and end-to-end organization in place and have invested significantly in doing so. Across the company, we have assigned the highest priority to making the necessary step-up in patient safety and quality management and have elevated leadership of patient safety and quality to Executive Committee level.

An integral aspect of quality is the ability to deliver and install equipment on time and to the required specifications. To this end, we are taking decisive action to make our supply chain more reliable and predictable, by securing near-term supply, redesigning and pruning our portfolio, and moving from a ‘one size fits all’ supply chain structure to a more agile, tailored value chain model per business, with dedicated and upgraded domain expertise. This will secure more deliveries, drive faster order-book conversion and build down inventory.

We are also simplifying the way we work to drive accountability and agility, with the aim of unlocking significant productivity and margin gains. This simplification – with end-to-end businesses with single accountability and more focused targets, supported by a much leaner enterprise layer, strong regions and a reinvigorated culture of patient- and people-centricity, innovation impact and clear accountability – is a primary enabler to drive flawless execution.

The set of measures we have taken includes the very difficult, yet necessary decisions announced in October 2022 to reduce our workforce by 4,000 roles globally, and then in January 2023 by a further 6,000, as we drive a major step-up in productivity. We will strive to implement these reductions with due respect for every employee affected and in line with all local rules and regulations.

We believe that, together, these measures will help us establish the culture, capabilities and infrastructure needed to consistently execute and deliver as a reliable patient- and peoplecentric health technology company.

Focused organic growth in Diagnosis & Treatment, Connected Care and Personal Health

As well as restoring our reputation as a responsible patient- and people-centric innovation leader in health technology, we urgently need to get back on course to create value with sustainable impact. To do this, we will drive organic growth through scale and leadership:

- Focusing investments to accelerate growth in Image Guided Therapy, Ultrasound and Monitoring, where we have strong #1 or #2 positions, and expand our leadership position in Personal Health
- Scaling our new Enterprise Informatics business
- Driving margin improvement in Diagnostic Imaging
- Restoring the Sleep & Respiratory Care business

We will leverage our distinctive market positions, especially our strong presence in North America and many international markets, while further localizing to support our leadership position in China.

Patient- and people-centric innovation at scale

We will continue to invest significantly in innovation, but are making a number of important changes to increase the impact of our patient- and people-driven innovation. Focusing our resources on fewer, better-resourced and more impactful projects, we will concentrate a higher proportion of our R&D resources in the businesses to ensure that innovation is done closer to our customers. We will scale and accelerate innovations, driven by the business and supported by rightsized corporate research, with patient safety, quality and sustainability at the core of innovation design. The technological and business model innovation that Philips brings to healthcare across care settings – often as part of long-term partnerships – is critical, making care delivery more convenient and sustainable.

2022 performance

Looking back on last year, sales increased nominally to EUR 17.8 billion, while several factors weighed down on profitability. Performance was impacted by our efforts to mitigate supply chain and inflationary pressures and the revenue and cost consequences of the Philips Respironics sleep recall, whilst at the same time dealing with global challenges such as the COVID situation in China, volatile demand and supply, and the war in Ukraine. As we worked through the operational challenges, we progressed on our execution priorities in the fourth quarter and saw initial signs of improvement.

I find it greatly encouraging that, despite our recent difficulties, Philips' purpose, strategy and solutions resonate strongly with customers, as evidenced by the around 100 long-term strategic partnerships we entered into with hospitals and health systems around the world in 2022, and by the continued strength of our order book.

Delivering on our ESG commitments

Environmental, Social & Governance (ESG) are three key dimensions defining our approach to doing business responsibly and sustainably. In 2022, we reached 1.81 billion people with our products and services, including 202 million in underserved communities – taking us a step closer to our goal of improving 2 billion lives per year by 2025, including 300 million in underserved communities.

We continued to work hard to deliver on our other key ESG commitments. For example, our updated carbon reduction targets were approved by the Science Based Targets initiative (SBTi), and we were included in CDP's climate action 'A-List' for the 10th year in a row. We see increasing momentum within the healthcare industry and on the part of our customers to reduce their environmental impact, and we are well placed – with innovations such as our BlueSeal magnet for helium-free-for-life MR and our Circular portfolio – to support that trend and help create a sustainable infrastructure for the future of healthcare.

Looking ahead

We remain cautious in light of the subdued economic outlook for the year, staffing and inflationary pressures facing our customers, geopolitical risks, supply and demand volatility, and uncertainties around ongoing consent decree negotiations, litigation and Department of Justice investigations. Nevertheless, we expect that, by prioritizing patient safety and quality, tightening our focus on innovation and strengthening our category leadership areas, while at the same time improving execution and taking a disciplined approach to capital, we will be able to progressively create value with sustainable impact. Against this background, and reflecting the importance we attach to dividend stability, we propose to maintain the dividend at EUR 0.85 per share, to be distributed in shares.

On behalf of the Executive Committee, I would like to acknowledge, once again, that 2022 has been very disappointing and we carry accountability for the plan to bring Philips back to where it belongs. I want to thank our customers and their patients for their understanding – and our suppliers and ecosystem partners for their support – over this past year. I appreciate our employees' hard work and willingness to embrace change and drive performance improvement. And I wish to thank our shareholders and other stakeholders for their continued support in these challenging times.

I am honored to have been tasked with leading our company and am heartened by the support I have encountered from our employees and customers, investors and other stakeholders. I am realistic about the challenges we face, but have full confidence in our plan of action and am firm in my resolve to lead Philips back to a position of strength in a world that needs meaningful innovation.

Roy Jakobs
Chief Executive Officer

