Philips Q1 2023 Results

Monday, 24th April 2023

Operator: Welcome to the Royal Philips First Quarter 2023 Results Conference Call on Monday, 24 April 2023. During the call, hosted by Mr Roy Jakobs, CEO, and Mr Abhijit Bhattacharya, CFO, all participants will be in a listen-only mode. After the introduction, there'll be an opportunity to ask questions. Please note that this call will be recorded and replay will be available on the Investor Relations website of Royal Philips. I will now hand the conference over to Mr Leandro Mazzoni, Head of Investor Relations. Please go ahead, sir.

Welcome

Leandro Mazzoni

Head of Investor Relations, Royal Philips

Hi everyone. Welcome to Philips First Quarter 2023 Results Webcast. I have here with me our CEO, Roy Jakobs, and our CFO, Abhijit Bhattacharya.

The first quarter press release and slide deck, as well as the frequently asked questions and deck on the Respironics recall, were published on our investor relations website this morning. The replay and full transcript of the webcast will be made available on the website as well.

Safe Harbour Statement

Before we start, I want to draw your attention to our safe harbour statement on screen. You will also find the statement in the presentation published on our Investor Relations website. In today's call, we will discuss our first quarter results as well as the progress on the actions we are taking across different areas to drive performance improvement.

With that, I would like to hand over to Roy.

First Quarter Highlights and Financial Performance

Roy Jakobs

Chief Executive Officer, Royal Philips

Key takeaways

Thanks, Leandro. Good morning everyone, and welcome. It's good to be with you again.

I want to start with giving you the key highlights for this quarter. First, we delivered a solid start to the year with 6% comparable sales growth and improvements in profitability and operating cash flow in Q1, as our actions to strengthen execution and to deliver shareholder value started to take effect.

Secondly, we are making good progress in executing our plan and on our three priorities: enhancing patient safety and quality; strengthening our supply chain reliability, which has helped our improved performance in Q4 last year and the first quarter this year; and establishing a simplified, more agile operating model.

Thirdly, resolving the Respironics recall for patients remains our highest priority. This quarter, Respironics recorded a €575 million provision in connection with the anticipated resolution of the economic loss class action in the US.

Looking ahead, based on our solid performance in the quarter, our order book and the ongoing actions to further improve execution, we are confident in our plan for 2023, acknowledging that uncertainties remain.

Solid operational performance as supply chain improves and actions to enhance execution start to take effect

Now, onto some key financials in the quarter.

We had a solid 6% comparable sales growth with strong growth of 15% in Diagnosis & Treatment, and 3% growth in Connected Care, partly offset by 6% decline in Personal Health. Comparable order intake grew double-digit in the Diagnosis & Treatment businesses, offset by Connected Care. Sales in the quarter were supported by the good momentum for Diagnosis & Treatment and Connected Care businesses in China as well. We see continuing strength of our order book, which is 10% higher than a year ago, despite strong revenue conversion in the last two quarters and a flat order intake in the quarter itself.

Adjusted EBITA margin was 8.6%, an improvement of 240 basis points compared to Q1 2022. Operating cash was an inflow of €202 million, a step-up of €429 million versus Q1 2022.

As you already know, Philips is a defendant in several class action lawsuits and individual personal injury cl aims. This quarter, Respironics recorded a €575 million provision in connection with the anticipated resolution of the economic class action in the US. Abhijit will provide more details around it. The anticipated resolution of the economic loss class action is an important step in addressing the litigation related to the recall. Visibility on potential outcomes on the medical monitoring class action and personal injury claims is not expected before 2024.

Demonstrating the confidence hospital leaders have in our innovation

Signed multiple new partnerships

I've met many of our customers and partners in the last three months, and it's absolutely clear that Philips remains a preferred innovation partner to help hospitals worldwide addressing their staffing shortages, enhancing productivity, and improve patient and staff experience. This has again been exemplified at events during the quarter. Philips Enterprise Informatics solutions resonated very strongly with customers at recent ViVE and HIMSS global healthcare events, which I attended.

We also had some key customer and innovation achievements in the first quarter. We signed a multi-year agreement with Northwell Health in the US, to standardise and centralised monitoring across the hospital, and we signed a multivendor services agreement with Prisma Health, also in the US, to become their sole source vendor for biomedical and clinical engineering services.

Highlights by Business Segment in Q1 2023

Diagnosis & Treatment

We expanded our leading ultrasound portfolio with the launch of the Ultrasound Compact 5500 CV, which facilitates first-time-right ultrasound exams for cardiology and vascular patients at the bedside.

Personal Health

In Personal Health, we introduced Sonicare for Kids 'Design a Pet Edition' to improve oral care habits among children. And we again achieved top ranking and medical technology patent filings at the European Patent Office, and we're included on the Clarivate top 100 global innovator list.

I'm very confident that our focused organic growth and scalable innovation strategy will further strengthen our businesses and results going forward.

With that, I would like to give the floor to Abhijit to take us through Q1 in more detail, after which I will come back on the progress on our execution priorities. Abhijit, please.

Financial Overview

Abhijit Bhattacharya

Chief Financial Officer, Royal Philips

Order book and order book coverage remain strong

Thanks, Roy. Good morning everyone. I want to start with our order book development in Q1, which ended 10% higher compared to last year, as Roy mentioned, driven by Image-Guided Therapy, Ultrasound, MRI, Monitoring, and Enterprise Diagnostic Informatics. Importantly, the margin profile in the order book reflects the price increases that we have been executing since last year, and will start running through our P&L from Q3 onwards.

Diagnosis & Treatment

Moving to segment highlights from the quarter, in Diagnosis & Treatment, comparable sales increase by 15%, driven by strong double-digit growth in ultrasound and Image-Guided Therapy and mid-single-digit growth in Diagnostic Imaging.

Sales grew double-digit across mature and growth geographies, with strong performance in North America, Western Europe and China. Order intake grew double-digit on the back of 7% growth in 2022. This was driven by strong double-digit order intake growth in Image-Guided Therapy and computer tomography, whereas Spectral CT 7500 continues to perform very well in the market.

Orders in growth geography grew by double-digit, driven by strong growth in China and Latin America. Orders in mature geographies grew by 3%, driven by 10% growth in North America. Adjusted EBITA margin increased to 11.3%, mainly driven by operational leverage, a better mix as well as productivity measures.

Connected Care

Connected Care comparable sales increased 3% driven by strong double-digit growth in Hospital Patient Monitoring, largely offset by Sleep & Respiratory Care. Order intake declined double-digit due to tough comps in Hospital Patient Monitoring on the back of the expansion and renewal of the install base during the period 2020 to 2022. For context, Hospital Patient Monitoring continues to run above pre-COVID levels, driven by the fundamental demand shift in adoption of our patient care management solutions and expanding market shares.

AI-powered patient monitoring is increasingly critical to care delivery. Our IntelliVue patient monitoring solutions are based upon superior hardware and predictive AI-based software that, together, monitor patients throughout their hospital stay.

Adjusted EBITA margin increase to 2.4%, driven by an improvement of more than 500 basis points of the Connected Care businesses, excluding Sleep & Respiratory Care.

Personal Health

Finally, in Personal Health, comparable sales declined 6% on the back of 8% growth in Q1 2022. This was due to a 4 percentage point impact from portfolio decisions related to Russia in 2022, and the lower consumer demand globally. Sales grew low single-digit in China, where we see improving sell-out trends.

Adjusted EBITA margin improvement driven by increased sales and productivity measures, partly offset by cost inflation

Adjusted EBITA margin was 13.2%, mainly due to the loss sales related to Russia. Adjusted EBITA margin for the group increased by 240 basis points to 8.6%.

Wage and component price inflation came in at around 300 basis points. However, this was more than offset by 120 basis points of operating leverage, and by our productivity and pricing actions, which contributed a further 520 basis points. The pricing impacts on our health system businesses – that is Diagnosis & Treatment and Connected Care – will be further reflected in the P&L during the second half of 2023 as we gradually convert more orders at new and better prices.

Productivity initiatives delivered €190 million in the quarter; €2.0 billion expected in the 2023-2025 period

Our productivity initiatives are on track. These actions delivered savings of €190 million in the first quarter. Operating model productivity savings amounted to €94 million. Procurement savings amounted to €32 million, and other productivity programs delivered savings of €64 million.

Restructuring, acquisition-related charges and other items in 2023

Adjusting items in the quarter included €150 million of charges related to the accelerated execution of the workforce reduction plan, where we are ahead of the plan with 5,400 role reductions to date. The full-year outlook for restructuring and acquisition-related and other charges remain in line with the guidance provided in January, except for the impact of the economic loss provision booked in Q1.

Let me provide you some more colour on that provision.

Resolving the recall for patients remains our highest priority

The provision was booked as Philips Respironics expects to submit a negotiated settlement agreement to the court for preliminary approval in the second quarter of 2023. While I cannot go into much detail of the provision at this moment, it's important to note that the economic loss resolution is being negotiated with the assistance of a court-appointed mediator as a potential class action settlement. That will resolve the economic claim loss claims of all device users, hospitals, and private insurers in the US, whether they've filed a lawsuit or not. Subject to final court approval, payments to class members under the settlement are not expected to begin until the first quarter of 2024 at the earliest.

With that, I'd like to hand you back to Roy.

Business Update

Roy Jakobs

Chief Executive Officer, Royal Philips

Resolving the Recall for Patients Remains our Highest Priority (continued)

Thanks, Abhijit. I would like to continue on the topic of the Respironics recall. We understand how important these sleep therapy devices and ventilators are for patients and how they improve their lives every day and night.

Resolving this has been and remains our highest priority. It's a complex, complex task, but we are making progress with some ups and downs. To date, more than 95% of the new replacement devices and repair kits have been produced and are ready to serve patients. The other 5% of the registered devices are primarily ventilators. Respironics is fully focused on working towards a solution. The vast majority of the produced sleep devices have been sent to patients and home care providers, and we are getting the remaining devices to patients as soon as possible.

Regarding the test and research programme, Respironics continues to expect to publish its toxicological risk assessment of the VOC emissions, resulting from ozone induced foam degradation in the DreamStation 1 devices, and to complete testing for System One and DreamStation GO sleep therapy devices in Q2. We are optimistic about what this news will mean for patients whilst we continue to work through the testing for ventilators.

Execution with decisive action as key value driver

To conclude, I would like to highlight some of the progress we have made in a quarter on our execution priorities.

Patient safety and quality as highest priority

First on patient safety and quality. To strengthen the voice of the patient, we established a new patient safety advisory board, which will be operational in the second quarter. To improve product quality, we added significant design control capabilities and talent in systems engineering and software design teams, and we are on track to deliver 45% reduction in the number of quality management systems this year, building on a 30% reduction by the end of last year.

If you look at corrective and preventive action systems, we'll continue to proactively identify issue, and we are increasing the number of investigations by design. This allows us to find and address them early. We are, of course, focused on this number to improve it significantly as we fully implement our plan.

Towards a reliable end-to-end supply chain

With respect to the supply chain, as of this month, we have moved to customer-centric, end-to-end supply chain teams closely aligned to the different businesses we operate in, and which we expect to further enhance efficiency level in delivering to customers. Several new dedicated leaders have already been announced for each business in the first quarter. We continue to make progress to reduce materials and component risks. For example, we have

accelerated the redesigns of components by completing 126 printed circuit boards compared to 56 as of the end of Q4, and we are on track to meet our target to de-risk all our high-risk components by year-end.

As you've seen in the results we have presented today, I'm pleased to see that these actions we have taken are already positively impacting our sales conversion rates.

Simplified, more agile operating model

Finally, we are simplifying our operating model by putting prime accountability into the businesses, supported by strong regions and lean functions.

As of this month, we have moved to end-to-end P&L accountable businesses. Our goal is to remove complexity and become more focused on strategy and innovation execution. This also included the difficult but necessary reduction of our workforce by 10,000 roles globally by 2025. To date, we have reduced 5,400 roles, and we are ahead of plan. This is accompanied by a significant change effort, and I want to thank and acknowledge the efforts of our employees, and thank them for the strong ongoing commitment to our purpose.

A leaner organisation will help Philips to become more agile and ultimately result in better outcomes for customers, consumers, and patients. This will also result in a simpler, more productive and more engaging workplace for employees who are motivated and attracted by our purpose. Moreover, since Q1, we are managing performance through reduced number of key operational metrics. We brought it down from 30 to 12, addressing customers quality, ESG and people, and financial performance. This focus allows us to make an impact in a vital field.

We are also strengthening our teams with new health tech talent, adding seasoned leaders with deep domain expertise, including to our Executive Committee. In addition to the changes announced in January, earlier this quarter, we announced the appointment of Julia Strandberg as the Chief Business Leader of the Connected Care businesses, effective today. Julia brings deep multidisciplinary expertise, including in informatics and monitoring, and in improving the healthcare experience for patients and providers across care settings.

Summary

Let me close out by repeating the key messages of the quarter.

We delivered a solid start to the year with 6% comparable sales growth and improvements profitability in operating cash flow in Q1, as our actions to strengthen execution and deliver shareholder value started to take effect. We are making good progress in executing our plan and on our three priorities: enhancing patient safety and quality; strengthening our supply chain reliability, which has helped improve performance in Q4 last year and the first quarter this year; and establish simplified, more agile operating model.

Resolving the Respironics recall for patients remains our highest priority. This quarter we continue to make progress on the remediation and Respironics recorded the provision in connection with the anticipated resolution of the economic loss class action.

Looking ahead, based on our solid performance in the quarter, our order book and the ongoing actions to improve further execution, we are confident in our plan for 2023, acknowledging that uncertainties remain.

I would like to thank you all for joining this call, and we will now take your questions.

Q&A

Operator: Thank you, sir. If any participant would like to ask a question, please press the star, followed by two times one on your telephone. Due to the time, please limit yourself to one question with the maximum of one follow-up. This will give more people the opportunity to ask questions. There'll be a short pause while participants register for questions.

The first question comes from the line of Hassan Al-Wakeel from Barclays. Please state your question, sir.

Hassan Al-Wakeel (Barclays): Thank you for taking my questions. I have a couple, please. So firstly, can you talk about guidance and why, after a very strong Q1, you've decided to keep guidance unchanged? How should we be thinking about the phasing of growth going forwards, given that guidance implies some slowdown sequentially? Is this more caution, rather than any real anticipation of a slowdown going forwards?

And then, secondly, you've noted that you've produced and shipped more than 95% of recall devices. Given the recent release by the FDA, which highlighted concerns that devices in the hands of patients were considerably less, could you talk about the deviation here, the expected time to get to patients as well as the broader relationship with the FDA? Thank you.

Roy Jakobs: Thank you, Hassan. So, first on guidance. So, we have said, and I'll just repeat, that we feel confident for 2023, based upon a combination of two things. One is we have on our own side, of course, the good and solid start to the year with this growth profile, the profitability and operating cash flow improvements, as well as that we see that the execution of the plan is taking effect. At the same time, we are early in the year, we don't want to adjust guidance every quarter and we also have uncertainties that we want to acknowledge that remain. And those are the same uncertainties that I called out earlier, which are macroeconomic, geopolitical and, of course, we have the CD coming. That's why we actually showed the confidence in the plan and have not further adjusted the guidance as a result.

On your second question, if I go to the recall. So we, of course, continue to put all our efforts on finalising the recall, and, as we shared, we're now at 95% of produced remediation devices, of which we have put the vast majority also into the hands of patients. If you refer to the callout, there is a gap between production and getting it into the hands of patients. If you currently look, in total, we have more than 4 million of the devices that are currently in the hands of the patients. So we're working through the rest, both in the US as in rest of world. That actually requires our efforts, but also the efforts of the patients, because some of the patients also still need to respond to some of the reach-outs that we have done to them. So that is really, really important for us to really finalise the remediation.

And then we have the respiratory care part that we also need to conclude upon, which I said we're working towards a resolution, and that's the remaining 5% of the total volume of the remediation.

And in terms of the relations with the FDA, we have continued strong engagement with them on multiple fronts. We're working through the remediation with them, we're working on the

CD, as you know, which we have made further progress, but we're not able to share the, kind of, status as per now because we have not yet reached an agreement. And we also made good progress on the testing, and, as I said, we aim to come forward relatively soon with the testing results, where we also got feedback from the FDA.

Hassan Al-Wakeel: No, that's helpful. And just in terms of the phasing of growth going forwards, how should we be thinking about that? And you talked about mid-single-digit expectations for D&T and Connected Care, with low-single-digit in PH. I wonder if that's changed at all.

Abhijit Bhattacharya: Yeah, I think – hi, Hassan, this is Abhijit – at the start of the year we had expected the year to be more second up-weighted. I think, with the way we have started, you will see a more smooth growth pattern through the year, so we don't expect a stronger than – second half as we had earlier guided for. And, if you look, our guidance on Connected Care and Personal Health, we don't see any reason to change, neither for D&T. But the good start for D&T gives us, let's say, more confidence that we will be on plan for D&T.

Hassan Al-Wakeel: Perfect. Thanks a lot.

Operator: Thank you. The next question comes from the line of Veronika Dubajova from Citi. Please state your question, madam.

Veronika Dubajova (Citi): Hi guys. Good morning and thank you for taking my questions. If I can just start with the D&T margin profile, Abhijit. Now, I'd just love to understand if there were any extraordinary contributors to that double-digit margin that you reported this quarter, and mix benefit and call out any contribution from pricing. Just, kind of, trying to get a sense of how representative this is of the underlying margin in the business and how durable it might be through the remainder of the year.

And then if I can just follow up on the litigation question that Hassan had asked about the FDA and – I'm really sorry, apologies – FDA question, not litigation question, that Hassan had asked. Are you still expecting the consent decree resolution this quarter? And any thoughts you have on the probability of outcomes and how those have changed as you've [inaudible]. Thank you.

Abhijit Bhattacharya: Hi Veronika, good morning. On the D&T margin, no, there were no special one-off positives in the margin in the first quarter. With the growth that we have, you get good operating leverage. Important, as you saw in the last couple of years, our high-margin businesses were the ones that were impacted; namely IGT and ultrasound. We have had very good growth in IGT and ultrasound, so that gives additional – let's say, that's why I put mix. Of course, the productivity savings that we have running across the company, D&T gets its fair share.

And then, regarding pricing, we do not see in Q1 and Q2, really, any significant pricing impact from the – from better orders that will come in the second half of the year.

Roy Jakobs: And let me take the second on the FDA and the consent decree. As I said earlier, we're in active dialogue on that and we have also next meetings planned. I would still hope for a quick resolution; I said earlier that that could be in Q2. Now, that's still something we definitely want to work towards, but as I also said earlier, we're not in control of that timeline and that's something, of course, that works together with the FDA. At the moment

we have clarity, we'll come forward, but I can assure you that we continue to work on that with great efforts.

Veronika Dubajova: Understood. And, Roy, any, sort of, change in your confidence in terms of that 2025 guidance and whether that's still consistent with the consent decree conversations you're having?

Roy Jakobs: No. I think there's no change on that perspective. I think, based on the start of the year, we are very confident on the 2023 year plan, both on the execution as well as, kind of, obviously coming through from supply chain. That allows us to say that, kind of, we have this confidence that has been growing in the quarter, based on this solid start of the year. Now, the consent decree is still one that we need to work through, but has not changed, in that perspective, the outlook for the year.

Veronika Dubajova: Okay, understood. Thank you, guys.

Operator: Thank you. The next question comes from David Adlington from JP Morgan. Please state your question, sir.

David Adlington (JP Morgan): Morning guys. Thanks for the questions. So, firstly, on – again, just on the D&T margin. I mean, going back in my model, about 10 years, normally the Q1 margin is low to mid single-digit, and you come in, obviously, more than double that. I just wondered if you can give us some help in terms of how we should be thinking about the margin progression through the rest of this year, and maybe just quantify how much of that is due to the cost savings versus the drop-through.

And the second question's on the balance sheet. Obviously, given today's provision, and you've got some costs coming up with the consent decree and personal litigation as well, I just wondered if you saw any need to strengthen the balance sheet? Thank you.

Abhijit Bhattacharya: Yeah. David, as I told Veronika, there's no special one-offs in the D&T margin improvement. I think, overall, a couple of things when you compare to multiple years back. The IGT share in the overall D&T mix has gone up significantly; now we are well above the €3 billion in terms of IGT businesses which are high margin. The cost, as you mentioned, and the productivity initiatives dropping, and we had mentioned that we wanted to get into the 12% to – sorry, into the 14-16% margin bracket for D&T. We had an unfortunate stall for a couple of years with all the supply chain issues that we had, and now that we are getting back on track, we see ourselves, again, getting to the guided ranges in the 2025 period.

Regarding the balance sheet, I think if you look, also, from the actions of the primary rating agencies, we are still – or we are a couple of notches above investment grade. There is no need to further strengthen it. Our cash generation starts the year off well and we are confident in the cash generation this year. And then once the settlement of the class action for economic loss comes, we also expect that to be offset by insurance money that we are likely to get. So therefore, we don't see any other actions to further strengthen the balance sheet at this time.

David Adlington: Great. Thank you.

Operator: Thank you. The next question comes from Delphine Le Louët from Société Générale. Please go ahead. Your line is open.

Delphine Le Louët (Société Générale): Thank you very much. Good morning, everyone. I was wanting to go back on the Chinese dynamic and as well as the North America dynamic. Can you be – can you give us a bit more granularity in this market, and especially regarding PH, to better understand what are the segments that are going fine? We had a lot of oral care last year. Can we have a comment on this one for PH and Chinese more locally about the trends and the take-up that you've seen, plus North America business, please? Thank you.

Roy Jakobs: Yeah. Let me – thank you, Delphine. Let me start. On China, I think we have seen China contributing strongly towards this quarter, especially on the Professional Health systems side. We still see the consumer side subdued. We expect that actually to strengthen from Q2 onwards. That's also actually in line with the expectations that we had earlier. So our outlook as we kind of started the year with, is actually coming through. And I would also say that we expect China to continue to have a strong contribution into this year. So we're happy to see China coming back, firstly, especially in health systems, but I think towards the coming quarters, we will see it also strengthening on the consumer side.

On the North American side, we have seen that also on the consumer side, we have seen subdued demand. We also expected that to be honest. So also earlier, we voiced that given the high inflationary environment, we just see that the volume is not coming through that there was earlier in the market. We're still holding strong in market share. So we don't believe that we are losing any traction with consumers that we have less attractive innovations. Actually, we get confirmation that they still are very much in the market for innovations, but it's just less demand.

Pricing is coming through on the consumer side. So actually, that helps us to kind of uphold, but there is impact. And as you also saw in the quarter, therefore, Personal Health is feeling those challenges. On the health systems side, in North America, we see that D&T was coming through strong, so that actually is a good development. We also see that actually in the mix certain choices are being made with customers, where actually they are now seem to be really getting back into both the IGT as well as in the imaging spaces, with some pent-up demand that we saw coming from COVID.

And as our supply chain strengthens, we are able to convert and actually go out to that in a better way. So that's, I think, the colour I can give.

Abhijit, I don't know if you want to add?

Abhijit Bhattacharya: Yeah. I think very important also add that, in China, as we see our local-for-local manufacturing going up, we then open ourselves also to get better order intake. So I think that is one.

Delphine, to your question on Personal Health dynamics in North America, it's important to understand that in the first two quarters of last year, we had high teens growth in Personal Health in North America. As you know, the post-COVID demand was coming back. So there, the comparables are tough. The market is not buoyant simply because of the factors that Roy mentioned on inflation, etc., but therefore, on the comparison, there is a decline.

And on China, we are glad we came back to growth in first quarter and with the high – or good sell-out that we see, gives us confidence on continuing the growth trajectory going forward in China, especially for personal health.

Delphine Le Louët: Okay. Can we have a quantification of the Chinese uptake in growth? How big was that for the whole?

Abhijit Bhattacharya: Growth of what?

Delphine Le Louët: The contribution to growth in revenue.

Abhijit Bhattacharya: For Philips? Or for –

Delphine Le Louët: Yeah.

Abhijit Bhattacharya: We had I think double-digit growth.

Delphine Le Louët: I mean, if you can give for PH share specifically would be fine.

Abhijit Bhattacharya: For PH, I mentioned first quarter was low single-digit. And then in the coming quarters, we will keep moving upwards. Because we see the sell-out being good, that means, of course, the distribution network will start restocking, and therefore, we expect that the growth will further accelerate during the year.

Delphine Le Louët: And for Philips, do we have any idea about the contribution of the whole of China in the growth?

Abhijit Bhattacharya: Yeah. So, I think we had good double-digit growth in the first quarter. It's about, what, 15% of sales. So there you can make your estimate.

Operator: Thank you. The next question comes from the line of Robert Davis from Morgan Stanley. Please state your question sir.

Robert Davis: Yeah. Thanks for taking my questions. My first one was just if you could give us a little bit more colour on the order dynamics within the Diagnostics & Treatment business. Obviously, we're seeing very strong sales growth. But I'd just be curious – given the current discussion around hospital CAPEX, etc., which I know you've provided in previous, I guess, slightly more cautious comments than some of your peers, I'd just be kind of curious to get your thoughts of what's going on there from an order perspective. Thank you.

Roy Jakobs: Yeah. Thank you, Robert. And just to provide more colour also building on what we said earlier, of course, in the D&T space, as Abhijit outlined, we have the IGT and the Imaging businesses. We see IGT, in particular, really starting extremely strong, and we expect that that also to continue.

In Imaging, it's a more diverse picture. We highlighted earlier that on MR, we still have more supply challenges, so we see that also being worked. So we are improving on supply, but still we are not there. And therefore, we also see some effect on the orders from that, whilst CT actually had a very strong start in the year. So the spectral CT, as also was outlined by Abhijit, is really making headway into the market. It's getting a lot of traction based on its improved imaging quality, but also the ease of use and using it in the workflow. So that's kind of, I would say, a bit of a mixed picture that we see across D&T. But overall, a very strong performance across the board.

Robert Davis: Thank you. And then just the other one I wanted to follow up is on your comments you made earlier, on the phasing of growth as you go through the year. I guess, given your backlog or your sort of order book coverage, I think, has sort of gone up again, what's the prospects for accelerating growth even more than you've seen in this quarter? Or have you kind of maxed out in this quarter? Is this the sort of fastest you can get stuff out of the door? Just trying to get a sense of how constrained Philips still is from just on the delivery side of things.

Roy Jakobs: Yeah, I think it's fair to say that this gives confidence that also actually the supply strengthening will continue, so I think you will see an overflow of this in Q2. So we were a bit more cautious in the outlook earlier, where Abhijit also mentioned that kind of we guided towards a slower start and second half will be stronger. I think now, as we were able to get better supply, and also we have the outlook on a continued stronger supply, I think you see that more evenly across the year. And this is something that, of course, depends on us; better supply gives us the ability to install. At the same time, we also need to work closely with our customers to get it installed and to get it planned for.

And as I shared earlier, of course, the climate is still pressured in the hospital environment, not only from a CAPEX environment but also just in terms of the people that they have to kind of operate the system. And it also means that there needs to be very careful planning with them to kind of work through the orders that we can convert.

Robert Davis: Thank you. Maybe just one final one. Just in terms of the profitability of the Connected Care business for this year, what are your sort of latest thought process there? Are you still sort of assuming breakeven just [inaudible] single-digit? Or given that it sort of started already, I think it was up to 2.4 in the first quarter, is there potential for that to get better as sort of sales accelerates over the year?

Abhijit Bhattacharya: Yeah. Look, typically, our Q1 profitability is our lowest. So typically, we will see Connected Care profitability increase during the year. The good news is that earlier where we were struggling with getting parts for patient monitoring, which is why we were impacted in profitability, that is now in a much better situation, so we start improving.

Also in Sleep & Respiratory Care, as we keep putting in the cost actions, you will see that we have guided to breakeven for the year. So, during the course of the year, that will increase. So yes, overall, you will see Connected Care profitability improving throughout the year, quarter by quarter.

Robert Davis: That's great. Thank you. Those are all my questions.

Abhijit Bhattacharya: Thank you.

Operator: Thank you. The next question comes from the line of Graham Doyle, UBS. Please state your question, sir.

Graham Doyle (UBS): Good morning, guys. Thanks a lot for taking my questions. Just one around sort of the consent decree and sort of recall and FDA. I just – we haven't had your take necessarily with regards to what the FDA put out 10 days ago around the nature of the language around the website and the recall. So it'd be good to get your sense as to sort of what's happened there in terms of the discourse[?] between yourself and the FDA?

And then I don't know if we should be looking at this as relevant for the ongoing consent decree. Or is it just something that's kind of cropped up alongside this?

And then one thing we haven't talked about, Abhijit, which would be quite interesting, is just around your take on the order book as we go through this year, because there's obviously, a point at which we would like [inaudible] the order book improve and grow and therefore indicate growth for 2024, 2025 on revenues. So just be good to get a sense as to when you guys have earmarked or are looking to see that sort of reflect. Thank you.

Roy Jakobs: Thank you, Graham. So maybe on the first in terms of the FDA mentioned or on – or asked to further clarify. I think what happened there is that we published, on our website, the amount of units that we produced. And as we are all focused, and in particular, of course, the FDA to know how many are with patients, they asked us to clarify how many were with patients. And at the moment that they published it, we had on the website, for example, that we kind of were at a production level of 2.5 million, which was the end of January number. But it was not clear enough on how many patients did receive, in the US, already their devices, which we, in the meanwhile, updated on the website, so we are clear on saying that actually, by now, we have produced 2.8 million of devices for the US, of which 2.2 million are in the hands of the patients. And we are working through the remainder to get them in the hands of the patients in this quarter.

So 95% of the total recall units have been produced. Out of that 95%, 4 million are with patients, so we're making good headway there and depends per country, what the percentages are. But what the call-out was of the FDA is be very explicit on how many are with patients, and that we clarified in dialogue with them as well on the website now and we updated that.

Abhijit Bhattacharya: Yeah, I think, Graham, on the order book, it's also important to know that not everything of our sales is in the order book. So there is 40% of our sales which is on recurring revenue. There is PH, which is not in the order book. And as I think Roy mentioned, very importantly, it also depends on customers when they are ready to take stuff and their sites are ready, etc. So the good news is that the order book is strong. The good news is that supplies are improving. And as we can work our way through that during the year, we will come back with how the year is progressing.

I think we mentioned that there are three uncertainties, whether it be macroeconomic – and there, we have seen what happened with the banks in Q1 or the inflationary pressures that are there. We have the geopolitical moves, which we are – which creates a lot of uncertainty and, of course, the CD, which creates uncertainty. So once we – till we have more certainty on some of these, we have – we currently hold to say that we have increased confidence.

Graham Doyle: Great. Thank you. Just one quick follow-up on the factors that led you guys to have a sort of confidence that we will get a Q2 consent decree finalisation. Have those factors changed? You said a little less [inaudible]. Or is it just a case of time has passed, and so there's just less time to the end of Q2, so naturally, you've got to be a little more cautious?

Roy Jakobs: I think it's the latter, Graham, right? We are working through it. As I said, I think we all want and aim to get to clarity around this. So – but at the same time, as we also said before, this is a diligent process and that we are working through. There are no further changes, in particular, to that.

Graham Doyle: Great. Thanks a lot, guys.

Operator: Thank you. The next question comes from the line of Falko Friedrichs, Deutsche Bank. Please state your question, sir.

Falko Friedrichs (Deutsche Bank): Thank you, and good morning. My first question is on the D&T business, and specifically on the organic sales growth in the first quarter. Could you quantify the volume and the price component for us?

Then secondly, on litigation. Can you provide a bit of a road map for us in terms of the medical monitoring class action and then the personal injury claims, just in terms of what we can expect here going forward in terms of the time lines?

And then thirdly, there were a couple of questions on that, but maybe you can summarise your thoughts on this hospital CAPEX environment in the US, given that you sounded a bit more cautious going into the year, printed very good Q1 results now. So what is your latest thinking regarding the outlook for the remainder of this year? Thank you.

Abhijit Bhattacharya: Hi, Falko. Let me take the first one and then, Roy, maybe the next two. So, on Diagnosis & Treatment, it's simple. I think the first quarter growth is primarily volume. Pricing is kind of negligible. As we said, pricing will flow more in the second half of the year, so you should see that primarily as volume growth.

Roy Jakobs: And on the litigation, so as we said earlier, so from a time line and road map perspective, we said that economic loss would be the first in resolving potential litigation claims. We also mentioned earlier that would be 2023, so we're happy actually that we see this now coming to fruition. We also mentioned earlier, and that actually has not changed, that clarity around personal injury and medical monitoring most likely will only be there from 2024 onwards.

So these processes are in much earlier stages than the economic loss. There's even the current discussion if there's a threshold value that actually goes into the case, so we are not changing any view on the time line for those.

And then on the hospital CAPEX in North America, I would have two comments there. One is I would say that I keep the same caution that North American market is still a market in which our customers have to deal with a lot. They still have staff shortages. There is still a high inflationary environment in terms of the cost that they need to operate with, still a lot of losses are being made. At the same time, we also see that they're making more clear choices. And therefore, the portfolio comes into play, where you saw that D&T because of less pickup during COVID and less ability to actually address those patients and also the technology there, is now I think in a catch-up mode; where, on the other hand, you saw some of the depression in monitoring, where actually you see that after two very strong years, they also look at kind of the current state of affairs for that business.

And whilst we expect that will continue, we also see there are certain new models that come into play, because our strong positions in North America also give us a lot of confidence that actually in the market, we are taking the share that's out there for us, and actually, we have very engaged dialogues. And I was at these two informatics, big events like HIMSS and ViVE. And here, you can just see how we all rally around, how can we help these hospitals with workflow solutions. And there, our unique enterprise informatics, kind of, positioning where

we have, both on the imaging side as well as on the monitoring side, unique propositions and leading propositions for interoperability and for remote care, that actually really gives a great strength and confidence.

We also announced the deal with Northwell, which is, of course, a very well renowned institute in the US. And we have many more that we have been engaging with, including some of the customers that came to the Netherlands to rally around long-term partnerships.

So, whilst on the overall environment we remain cautious, we are very active with the North American customer base and our portfolio, and, therefore, also remain confident in future outlook and positioning for us in North America.

Falko Friedrichs: Okay. Thank you.

Operator: Thank you. The next question comes from the line of Sezgi Biçe Özener from HSBC. Please state your question, madam.

Sezgi Biçe Özener (HSBC): Hi. Thanks for taking my questions. I also have a few, please. First one, a technical one. Can you describe the difference between the regular recall provisions, as well as the remediation provisions that you set aside?

And second of all, could you specify how much the cash inflow from the real estate sale was and whether that has any impact on the P&L as well?

And my last one, please. On the remaining 5% of ventilators, you said you're still working on a solution. Can you give an idea on how the solution differs from the others on that front?

Abhijit Bhattacharya: Yes. I'm not clear about the question on the difference between the recall provision and the remediation, but maybe let me try to explain it. And if it's not clear, then please let me know, Sezgi.

Sezgi Biçe Özener: Sure.

Abhijit Bhattacharya: But there are two actions. One is the whole action around the remediation. So that is the repair and replace programme, right? So we had these sleep apnoea machines and ventilators, which we – which needed to be repaired or replaced. That was the provision that we took for the last couple of years. This – the class – the economic litigation provision – the economic loss litigation provision is specifically related to cases that were filed – the class action case that was filed against us. And this is an amount which we think is our best estimate at how much we will have to settle. So that's the difference between the two types of provision. One is our cost to repair and remediate; the other is what we will have to pay to plaintiffs.

Sezgi Biçe Özener: Okay.

Abhijit Bhattacharya: Then on the real estate, it's not a significant amount, but it was one of the contributors, but it's not a very big amount. We are not going to give specific amounts on a transaction, but it was not so significant. And then maybe on the ventilation one, I talked about…

Roy Jakobs: Yeah. So on the – so what we mean with solution. Of course, we have different ventilator types that we are working towards a solution type by type. You might have seen that we had a setback in the Trilogy 100/200. We're kind of resolving that and

coming forward with a new solution. The same for the A series. So that's kind of what we mean with kind of working through the appropriate solution for the ventilators.

Sezgi Biçe Özener: Thanks very much. That's helpful.

Operator: Thank you. The next question comes from the line of Wim Gille, ABN AMRO-ODDO. Please state your question, sir.

Wim Gille (ABN AMRO-ODDO): Yes, very good morning. Wim Gille from ABM ODDO. I've got two in fact. First, if I look at the outlook, and I know the question has been asked multiple times. But if you look at the outlook that you have for the year with high single-digit margins, and then if I look at the margin that you had in the first quarter, which is ahead of the average margin that you produced in the last decade in the first quarter. And meanwhile, we see that the positive pricing impact is still to come through. Meanwhile, we see that PH, which is your most profitable division, actually should see an improvement going out through the year. So what is kind of holding you back from updating the margin expectations already today?

And my second question would be on, let's say, the works council in the local press here in the Netherlands, they're stating that the works council on the central R&D teams are planning to dispute the layoffs in the – on the [inaudible]. I don't know how to translate that. But can you – it's a bit of an unusual step, so can you give us a bit more clarity on that one? Thanks.

Abhijit Bhattacharya: Yeah. Hi, Wim. So on the outlook, yes, I think we have said that we are actually glad with the strong start to the year, but Roy also mentioned a couple of times, and so did I, that we have uncertainties as well. And till we have more certainty around a few things, we are not going to be changing our guidance every quarter. If there is a particular event that happens, that allows us to get more certainty around the uncertainties we have flagged, we would change our guidance. But without that, frequent revision of guidance is something we are not going to do at this stage.

So let me leave it at that and then maybe Roy, you take the workers' council question.

Roy Jakobs: Yeah, let me – so on the workers' council, so I think it's good to understand, of course, we are working through various workers' council to get all the different parts of the reorganisation kind of worked through diligently with them because these are impactful changes. One workers' council, which is in the area of innovation, has put forward to the [inaudible], indeed, a request to validate our request. This should be seen as a procedural right they have.

It's also good to know actually, they are not active on that right. They have put it in, but as we are in productive dialogue, they have not asked the judge to actually explore this yet actively. So this is just preserving their rights. It's part of a process right that they have. But most importantly, we are working together with them strongly to kind of to get to an agreement on it.

I also want to stress that, of course, I appreciate that changing the innovation model, like we do, is a big change for the affected employees, especially if you have been working so hard in corporate research for long, delivering a lot of good results to Philips over a long period. But we need to get current in our innovation model, and therefore, the step that we're taking to bring it closer to customers, to get the clock speed up, and therefore, to get more impact

from the innovations is the right one that we will further pursue in collaboration, of course, with workers' councils.

Wim Gille: Thank you.

Operator: Thank you. The next question comes from the line of Julien Ouaddour from Bank of America. Please state your question, sir.

Julien Ouaddour (Bank of America): Good morning, and thank you for including me at the end. So just one for me. Over the past quarter only, we've seen the number of personal injury claims going from 20,000 to 40,000 as more people joined the census registry. Just what are your projections in terms of the number of claims going forward? And does the higher number of plaintiffs implies higher potential settlement amounts for you? Thank you.

Roy Jakobs: So it's – so on – so just to – on the personal injury claims, the number has gone up to 40,000. But actually, this is something that – and just to clarify, so we have 400 claims, and we have 40,000 people that are in the census registry. So they have not yet filed any claim. They hold the right as part of the registry to go into a claim. And actually, that number has only slightly gone up over recent periods. So that's something that, kind of, we, of course, are watching, but it's not something that has been a material development that actually has concerned us.

I think what is important for us, of course, we are working towards finalising of the testing. As I said, we will come forward with testing hopefully soon in Q2, in particular on the sleep ozone testing that we owe you the results and on DreamStation go, so that we can complete the full sleep testing. And that would also help in these cases. But to confirm that actually this is not a material development, the 40,000 in the census registry, and we have 400 files that are, kind of – 400 claims that actually are filed in personal injury.

Julien Ouaddour: Okay, thanks. I had just in mind that you had 20,000[?] people like in January. So that's why I thought like the number has doubled over the – like the last three months.

Roy Jakobs: No, no. So actually, there's not a significant increase on that number. We already had – earlier we were above the 30,000 number. So that's something that was not a significant uptake in this quarter.

Julien Ouaddour: Okay, perfect. Thank you.

Operator: Thank you. Gentlemen, that was the last question. Please continue.

Roy Jakobs: Thank you so much for all your questions. As said, this, I think, is – has been an encouraging start of the year, where we presented to you that we have solid growth, improved profitability and improved cash flow. As well as we're making good progress on our execution, in which I think the most material news was that we have provided for an economic loss class action. As well as that we're making good headway in getting more supply to underpin the year. As well as also making sure that we get the productivity savings as a result of the actions we take on cost side, including reduction of force. And that has led us to, kind of, be confident in our plan for the remainder of the year.

Thank you for your attention and talk to you soon.

Operator: This concludes the Royal Philips' First Quarter 2023 Results Conference Call on Monday, 24th April 2023. Thank you for participating. You may now disconnect.

[END OF TRANSCRIPT]