

PHILIPS



Q2 2023 Results

Monday, 24th July 2023

Operator: Welcome to the Royal Philips Second Quarter and Semi-Annual 2023 Results Conference Call on Monday, 24th July 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 Philips – of Royal Philips. I will now hand the call over to Mr Leandro Mazzone, Head of Investor Relations. Please go ahead, sir.

Preamble

Leandro Mazzone

Head of Investor Relations, Royal Philips

Hi, everyone. Welcome to Philips second quarter and half-year 2023 results webcast. I have here with me our CEO, Roy Jakobs, and our CFO, Abhijit Bhattacharya. The second quarter and half-year press release and slide deck, as well as the frequently asked questions and deck on the Respiroics recall, were published on our investor relations website this morning. The replay and full transcript of this webcast will be made available on the website as well.

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 results as well as the progress on the actions we're taking across different areas to drive performance improvement.

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

Second Quarter Highlights

Roy Jakobs

Chief Executive Officer, Royal Philips

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

Key takeaways

I want to start with the five – or with the key highlights for this quarter. First, we delivered an improved operational performance, with 9% comparable sales growth and improvements in profitability and operating cash flow. The improvements were across the company, with all business segments and all regions contributing. These positive results are results from our ongoing actions to strengthen our execution.

Secondly, we are making progress in executing our plan and all our three priorities: enhancing patient safety & quality; strengthening our supply chain reliability, which supported our performance in Q4 last year and the first half this year; and establishing a simplified, more agile operating model, supporting our productivity.

Thirdly, resolving the Respiroics recall for patients remains our highest priority. The vast majority of the sleep therapy devices are now within the hands of patients and care providers,

and the complete testing and analysis for sleep devices affected by the recall showed positive and reassuring results for patients.

Looking ahead, based on our strong performance in the first half of the year, our order book and the ongoing actions to improve execution, we have raised the outlook for the full year 2023. Whilst acknowledging that uncertainties remain, we now expect mid-single-digit comparable sales growth and adjusted EBITA margin at the upper end of the high single-digit range.

Improved operational performance driven by sales growth and focus on execution, order book supporting growth for next quarters

Now, on to the key financial highlights in the quarter. We had a strong comparable 9% sales growth. Diagnosis and Treatment grew 12%, Connected Care grew 6%, and I'm encouraged by the return to growth in Personal Health.

Our adjusted EBITA margin was 10.1%, a strong improvement of 490[?] basis points compared to Q2 2022. Operating cash saw an inflow of €135 million, a step-up of €440 million versus last year. Our order book increased 3% year-on-year, even after strong order-book-to-sales conversion of the last three quarters. I'm confident that this order book will continue to support sales growth in the coming quarters.

On the back of the high order intake in Q2 2022 and Q1 2023, comparable order intake declined 8% in the quarter. Excluding Russia, this would have been 4%. This confirms our earlier view that orders would be lumpy as we work hard to deliver order intake growth in the second half of the year. This is founded upon strong fundamentals of the markets in which we operate, as they remain strong, and I'm very confident that our innovation portfolio is well positioned to help hospitals worldwide address their staffing shortages, enhance productivity and improve patient and staff experience. The order funnel remains healthy, and we see signs of improvement in cost inflation and staff shortages in hospitals compared to 2022, but we also continue to expect hospitals and healthcare systems in the US and other mature geographies to exhibit cautious buying behaviour in the short term, given the global macroeconomic conditions.

Enterprise Monitoring as a Service agreement with University of California Irvine Health

During the second quarter, we achieved some key customer and innovation milestones. We signed a multiyear agreement with University of California Irvine Health to provide, to provide enterprise monitoring as a service, including informatic solutions to standardise, centralise, and scale monitoring across the health system.

Highlights by business segment in Q2 2023

Five top hospitals in Shanghai, with more than 10,000 beds, installed the Spectral CT 7500. We also expanded our leading Image-Guided Therapy portfolio with the launch of Zenition 10, a cost-effective mobile imaging system to guide high-volume routine surgery as well as complex orthopaedic and trauma procedures.

We introduced the cloud-based Philips Health Suite Imaging PACS on Amazon Web Services, designed to enhance image access speed, reliability, and data orchestration for clinicians across the imaging workflow.

In Personal Health, we launched a premium 7 Series shaver in China, in partnership with JD.com, which debuted as the number-one shaver on this online channel.

With that, I would like to give the floor to Abhijit to take us through Q2 in more detail, after which I will come back on the progress on our execution priorities. Abhijit, please.

Financial Performance

Abhijit Bhattacharya

Chief Executive Officer, Royal Philips

Thanks, Roy. Good morning, everyone.

Diagnosis & Treatment

Let's begin by looking at the segment highlights from the quarter. In Diagnosis & Treatment, comparable sales increased by 12%, driven by strong double-digit growth in Ultrasound and Image-Guided Therapy and mid-single-digit growth in Diagnostic Imaging. Adjusted EBITA margin was 10.6%, an increase of 380 basis points over last year, mainly driven by operational leverage, a favourable mix, and productivity measures. The profitability sequentially was impacted by mix and cost phasing. In the first half of the year, adjusted EBITA margin was 11.8% for Diagnosis & Treatment, an increase of 460 basis points compared to the same period last year. This, together with our productivity, pricing actions, and order books, gives us confidence for the coming quarters.

Connected Care

Connected Care comparable sales increased by 6%, driven by double-digit growth in Monitoring, partly offset by Sleep & Respiratory Care. Adjusted EBITA margin was 7.5%, an increase of 570 basis points, driven by productivity measures and a significant improvement in the profitability of monitoring.

Personal Health

Personal Health returned to growth with 3% comparable sales increase, which is encouraging. Consumer demand remains subdued globally, as we expected, but there is evidence of gradually improving sellout trends. Adjusted EBITA margin was 13.4%, an increase of 100 basis points, driven by pricing and productivity measures.

Adj. EBITA margin improvement driven by increased sales, royalty income and productivity measures, partly offset by cost inflation

Adjusted EBITA margin for the group increased by 490 basis points to 10.1%. Wage and component price inflation came in at 260 basis points. However, this was more than offset by 150 basis points on operating leverage and by our productivity and pricing actions, which contributed a further 580 basis points. Additionally, the Q2 adjusted EBITA included a positive impact from phasing of royalty income, in line with the guidance we provided for the segment 'Other' for the quarter. We continue to improve our cash flow, with a significant year-on-year improvement. This has delivered an improvement of the leverage from 3.6% to 3.1 – sorry, from 3.6x to 3.1x adjusted EBITA in the first six months of the year.

Productivity initiatives delivered €237 million in the quarter and €427 million year to date

Our productivity initiatives are on track and delivered savings of €237 million in the second quarter. Operating model productivity savings amounts to €112 million; procurement savings was €57 million, and other productivity programmes delivered €68 million of savings. Adjusted items in the quarter included €161 million of charges, mainly related to accelerated execution of the workforce reduction plan, with 6,600 role reductions to date out of the planned reductions of 7,000 roles for the year and 10,000 roles to 2025.

Strength of our order book to fuel growth in next quarters

Moving to our order book, which ended the second quarter 3% higher compared to last year, it's worth noting that this is significantly higher compared to the period before the global supply chain constraints, even after the strong order-book-to-sales conversion over the last three quarters. Orders and order books are an important leading indicator for around 40% of our revenue. The remaining 60% comes from recurring revenue such as services and consumables from book-to-bill business and from Personal Health. As you can see at the bottom of the page, the absolute levels of order intake remain healthy, but we see a steep increase in sales levels, year-to-date, due to enhanced order-book-to-sales conversion following supply chain and execution improvements.

Order intake decline on the back of high comparison base and Russia; strong effort in place to reverse the trend in second half of the year

In Diagnosis & Treatment, comparable order intake declined 8%, or -2% excluding Russia. This follows the double-digit comparable order intake growth in Q1 2023 and the high order intake in Q2 of 2021 and 2022. Overall order intake in Diagnosis & Treatment was mid-single-digit up, excluding Russia, following a mid-single-digit order intake growth in the first half of 2022. The Russia impact is due to longer lead times because of initial export control procedures in place since this quarter.

Order intake declined 7% in Connected Care in the second quarter due to the tough comps in hospital patient monitoring after the expansion and renewal of the installed base during the period 2020 to 2022. For context, Connected Care orders continue to run at levels double digits higher than pre-COVID, driven by fundamental demand shift in adoption of our patient care management solutions and expanding market shares.

Raised outlook for FY 2023 driven by confidence in the execution of our plan, while uncertainties remain

As Roy mentioned, we have raised the outlook for the full year 2023. Whilst acknowledging that uncertainties remain, we now expect mid-single-digit comparable sales growth and an adjusted EBITA margin at the upper end of the high-single-digit range. We expect to carry the positive momentum into the second half of the year while facing tougher comparison base in the fourth quarter.

Restructuring, acquisition-related charges and other items in 2023

The full-year outlook for restructuring, acquisition-related, and other charges remain in line with the guidance provided in January, despite some shifts between the different cost buckets based on year-to-date results.

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

Delivering Value with Sustainable Impact

Roy Jakobs

Chief Executive Officer, Royal Philips

Resolving the recall for patients remains our highest priority

Thanks, Abhijit. I would like to continue on the topic of the Respironics recall, which has been and remains our highest priority. Today, around 99% of the new replacement devices and repair kits have been produced. Over 4.5 million of the produced sleep devices are now in the hands of patients and homecare providers, while the remediation of the affected ventilators is ongoing. Regarding the test and research programme, Respironics has published complete testing and analysis for Dream Session 1, Dream Session Go, and System One sleep therapy devices in Q2, which showed positive and reassuring results for patients. We continue to work through the testing for ventilators.

As previously discussed, the litigation investigation by the US DOJ related to the Respironics field[?] action, as well as the discussions on the proposed Consent Decree, are ongoing. We are also in continued dialogue with regulators across our key markets on how to service new patients going forward. I am confident that our focused growth strategy for scalable innovation will further strengthen our businesses and results going forward.

Execution with decisive action as key value driver

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

Patient safety and quality as highest priority

First, on patient safety and quality. Our new Patient Safety Advisory Board went live in the quarter, driving deeper engagement with patients, healthcare professionals, and industry experts. We continue to add significant capabilities and talents across the businesses. For example, we appointed strong Regulatory Affairs and Quality leaders to the newly formed Enterprise Informatics business. Patient safety quality reviews are fully embedded in the new performance management cadence, and we remain on track to deliver 45% reduction in a number of Quality Management systems this year, building on a 30% reduction by the end of last year.

Towards a reliable end-to-end supply chain

With respect to supply chain, as of the second quarter, we have moved to customer-centric end-to-end teams, closely aligned to the different businesses we operate. We continue to make progress to reduce materials and component risks, although challenges remain. For example, we have accelerated the redesigns of components by completing 160 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 have seen in the results we have presented today, I'm pleased to see that the actions we have taken continue to positively impact our sales, as well as our service levels.

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. This also included the difficult

but necessary reduction of our workforce by 10,000 roles globally by 2025. To date, we have reduced 6,600 roles, as mentioned by Abhijit. I want to express my gratitude to all my Philips colleagues for their dedication and commitment to deliver results as we create a more focused and agile organisation. We are also strengthening our teams with new health tech talent, adding seasoned leaders with deep domain expertise across businesses, regions, and functions. Year to date, close to 300 talents with a health-tech background joined our organisation.

Key takeaways

Let me close out by repeating the key messages of the quarter. We delivered strong operational performance in Q2, with 9% comparable sales growth and improvements in profitability and operating cash flow. We are making progress in executing our plan and on our three priorities: enhance patient safety and quality, strengthen our supply chain reliability, and establish a simplified, more agile operating model. Resolving the Respiroics recall for patients remains our highest priority. And looking ahead, based on our strong performance in the first half of the year, our order book, and the ongoing actions to improve execution, we have raised the outlook for the full year 2023, acknowledging that uncertainties remain.

I would like to thank you for joining the 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 a maximum of one follow-up question. This will give more people the opportunity to ask questions. There will be a short pause while participants register for questions.

We will now go to your first question, and it comes from the line of Hassan Al-Wakeel from Barclays. Please go ahead.

Hassan Al-Wakeel (Barclays): Good morning. Thank you for taking my questions. I have three, please. Firstly, on the guidance upgrade, can we read anything into your Consent Decree assumptions that you've embedded into guidance and whether they've changed at all over the last two to three months? Is the delay driving any meaningful guidance benefit, and is it fair to assume that your central case is not a Respiroics-wide injunction?

Secondly, and also on guidance, your new guidance implies a step-down in growth in the second half and no real improvement in margins sequentially, despite productivity and pricing benefits, as well as higher absolute revenues in the second half. So what's driving your caution here?

And then finally, could you talk about your return to market in CPAP outside of the US and whether you're in discussions with regulators, and what the process is here? Do you expect to return to other markets in the second half of this year? Thank you.

Roy Jakobs: Thank you, Hassan. Let me start with taking your first question. So, in terms of the guidance and whether there's anything to read into – to the CD, so actually we have not adjusted any CD assumptions, as we are still in discussion on the CD and, as we don't

want to speculate on any outcome, we also have not touched any of the underlying CD assumptions. What we have looked at is the underlying improvement of our business and, as you have seen, based on a strong Q1, strong Q2, and also the fact that the actions we are taking are yielding their results in terms of getting more supply to convert our order book that is strong, as well as driving productivity – that has been the reason why we, kind of, have upped the rate for the full year and of the guidance.

We have also said that uncertainties remain. That's something that we have been saying from the beginning of the year. We are still living in quite a, kind of, dynamic macroeconomic environment, so that's something that we keep on the back of our minds that we, kind of, also are ready to, kind of, address any of those dynamics that could happen also in the second half. But we, of course, remain fully focused to carry the good momentum through into the second half, but also do have some tougher comps that will kick in, especially in Q4, as that's the moment that we turned back into growth last year and that we have, of course, been able to pull through in Q1 and Q2.

And that's, in essence, combining, I would say, the answers in your first and second question. Then, in return to market out of US, so we are indeed in discussion with regulators, as we are also now completing, especially on the Sleep side, the recall in many markets. We have made great progress there, and that then also leads to the subsequent discussions on how and when to return to growth. So, that's something that we will see probably materialise further into second half, and we'll keep you updated the moment that we have any further news there.

Hassan Al-Wakeel: That's helpful. Roy, I guess, if I can just follow up on the CD, I mean, you state that you're in advanced discussions, and you have received drafts, even in the recent months. Have your discussions with the FDA changed at all, and is it fair to assume that your central case, which you embed within guidance, is not a Respironics-wide injunction?

Roy Jakobs: Hassan, as I said earlier, we do not speculate on the outcome of the CD, as many variations are possible. I can continue to stress that we are in active dialogue with the FDA; that remains ongoing. There's also no specific reason, kind of, for a, kind of, further time lag[?] on that. We want to get it, of course, resolved as soon as possible, as does the FDA, with the patients' interests in mind, but it also is fair to say that these are important and detailed discussions that are happening, and that's why, kind of, we continue to progress on those.

Hassan Al-Wakeel: Perfect. And, sorry, a final one just to follow up on the margin commentary. Just given the strength in Q2 and the impact from workforce reduction, how far are we through that in terms of the realisation of benefits, and what should we expect for the remainder of the year? Thank you.

Abhijit Bhattacharya: Hi, Hassan. This is Abhijit. Good morning. We've been moving at a pretty good pace in terms of our reduction of headcount. So we just said that we've done about 6,600 of the 7,000 planned for the year, so that should give us a benefit going into the second half. The general plan was roughly – we had 3,000 last year. The plan was 4,000 this year, evenly split through the quarters. So we are slightly ahead and are confident of making that plan. So I think that's where I would leave it.

Operator: Thank you. We will now go to your next question, and your next question comes from the line of Veronika Dubajova from Citi. Please go ahead.

Veronika Dubajova (Citi): Hi, Roy. Hi, Abhijit. Hi, Leandro. Thanks so much for taking my questions. I have two, please. The first one's just going back to the guidance. I mean, if I just look at the mid-single-digit growth guidance that you've given for the year against the delivery in the first half, it does imply pretty significant deceleration in growth into, sort of, flat to low-single-digit range. Just want to understand, is there anything that you're seeing at the moment that makes that a likely outcome, or are you just embedding a degree of conservatism? And if you can maybe talk through – I don't know, I know July has barely started, but just maybe comment on what you're seeing in the quarter to date against that guide. That would be helpful.

And then my second question is on the order book momentum. And clearly, pretty significant deceleration here versus what you delivered the prior quarter. I appreciate there are some difficult comparisons in there, but I – just maybe curious to get your thoughts, or, I mean, if I look across your performance and your peers' performance, we are clearly seeing some slowdown in order growth this year. Just, kind of, put it into context for us, because at the outset of the year, I think everyone was pretty excited about China. That's growing pretty healthily, from what we understand. So is this a problem in the US, is this a problem in Europe, is this a problem somewhere else? Kind of, what gives you the confidence that this can improve as you move into the back half of the year and that it can support that, sort of, mid-single-digit growth in the D&T and Connected Care businesses that most of us expect for 2024? I know there's a lot of moving parts there, but if you can just give us a little bit of that, that'd be helpful. Thank you.

Abhijit Bhattacharya: Hi, Veronika. Let me take the first part of the question. I think if you look – if you take a step back, we had planned for actually a back-end-loaded year. We ultimately saw that the supply chain improvements came in earlier, and therefore we have had a strong start to the year. As you've seen, in the second quarter, our good growth was a bit flatter also because of our royalty income. So, if you take that into account and look at the second half, you see good momentum going into the third quarter, but also you should remember that in the fourth quarter, we are battling tougher comps. If you remember, last year in the fourth quarter, health systems businesses grew mid-single digit, so, of course, therefore the growth will be – let's say, the year-on-year growth in the fourth quarter would not be as strong as it has been for the first two quarters this year.

So that's the colour I can give you on how we expect growth to play out for the remainder of the year. It's not that there is a specific issue or something that we want to signal at all. We need to just get through quarter by quarter. The supply chain improvements have happened, but it's not over, so we are still working these through, and as we get through every quarter, hopefully, we are able to deliver in line with the commitment.

Coming to your second question, maybe I hand it over to Roy.

Roy Jakobs: Yeah. I think – Veronika, thank you for the question. And on the order book, indeed, I think important a few parts to take together. First of all, as we highlighted, we have still been growing versus last year, so it's really important to recognise the strength of the order book that we have. And actually, we are still challenged to burn it down faster, so

actually that is one area that we also want to work through. And that's where this remaining focus on getting more supply to be able to deliver more of the products actually will help us to deliver also better to customers, and then also take more orders into our order book.

Secondly, there is indeed a certain lumpiness. I started the year with saying that this is not a business-as-usual year. Now, I've been talking to many customers. I've been – a few weeks ago, I went to China. China actually is coming back very strong, as you have seen. That started already Q1; it continued Q2. We actually see it continuing in Q3 and Q4. So we can expect, I think, a double-digit contribution out of China for this year, and that's great to see China coming back. We also saw now in the Q2 that Personal Health came back into growth. That's also important momentum that we will continue into third and fourth quarter.

But I also went to the US, and actually, I was there even last week. I've been talking to customers also there, and I must say that I've been encouraged by some of the signs that I'm seeing, when talking to customers, that there is some stabilisation coming in [inaudible] challenges. So, whilst there's still challenge on it, actually they seem to be finding resolutions. We're also helping them with that with our technology and innovations. That's what we're also talking about. And also, they're combating the inflation, I think, more effectively.

So that's what I would also take into the second half, where actually I would expect that the order intake would see growth coming back into play, and that will then not only be growth of the absolute order book but also in order intake. And we will work hard for that across the globe.

And that's maybe the last piece. I think what I was also happy about is that, kind of – you saw that our contribution into the growth delivery in this quarter came from all businesses and all regions, which also means that there is no specific, kind of, part that is laying back or, kind of, is behind. So Personal Health was the one that was still not as strong as we hoped for in the first, kind of, half. We knew it; we expected that. So now we hope to continue the growth momentum across all segments into the second half.

So there is no, I would say, specific reason for caution or for concern, but we remain at the same time realistic that this not a business-as-usual year and that our customers, and also the world, is working through the current inflation, the interest and the challenges that are in the labour market.

Veronika Dubajova: And can I just ask a quick follow-on, Roy, just on the Consent Decree? I think before you had talked about you had hoped to get it resolved and settled in the first half of the year. I might have missed it, but I didn't see a comment on the updated timeline in the press release this morning. Do you have any thoughts on when we might see a resolution there?

Roy Jakobs: No, I've not, so that's also why we did not put a timeline in. So, and I also don't want to further speculate on it. I think it's important to stress that also there, there's no specific reason that I would call out or any specific concern that this is indicating something. I think it only indicates that this is being worked through very diligently and at the same time, as I said earlier, there's a lot happening across the plate of both the FDA but also on our side. So I think both parties, we are putting all our efforts into it to bring this to the best possible conclusion. The moment we will get any update on timing or conclusion, of

course, we will come forward with it. But it's hard to put a specific timeline on it. Also, when I said earlier in the year I would hope for first half, indeed, that was my hope, but I also said it's not in our control as, yeah, there's a lot to be worked through and that's, kind of – yeah, we have seen materialising now.

Veronika Dubajova: Understood. Thank you guys so much.

Operator: Thank you. We will now move to our next question and the question comes from the line of Richard Felton from Goldman Sachs. Please go ahead.

Richard Felton (Goldman Sachs): Good morning. Thank you for taking my questions. My first one is on Connected Care. So look, strong performance on the margin, which drove the beat at group level in Q2. But could you provide a little bit more colour on the margin drivers within the division, please? I'm specifically interested to know the impact from Monitoring versus Sleep and Respiratory Care. And then were there any one-offs which drove strong performance in the quarter for Monitoring? That's my first one.

And then my follow-up, also on Connected Care. Look, it looks like Sleep and Respiratory Care still had a fairly material revenue decline in Q2, but given the system sales were, I think, already zero last year, could you provide a little bit of colour on where those incremental declines are coming from, please? Thank you.

Abhijit Bhattacharya: Yeah. So, hi Richard, this is Abhijit. On Connected Care, as we mentioned also in the commentary upfront, it's coming mainly from monitoring. We have had a – it's a very profitable business and Monitoring, as you would remember, last year was really hit by the component situation. I think we have had a 20+% growth in the second quarter, and then when you get operating leverage, of course you get a big impact.

Besides that, in Sleep and Respiratory Care, also we had started in Q1 taking cost actions, so therefore, there the profitability starts to improve. So, I think overall it's pretty much organic, so there are no real one-offs.

Roy Jakobs: Maybe I can take the second one on the SRC side. So, if you look to the SRC mix, actually you see that the Ventilation side was where we saw the decline. We're also still working through the remediation on that, so actually, that is connected. But at the same time, if I look to Masks, actually we have seen Masks coming back stronger and that was a positive development in the quarter. So, it's a mix issue, where the Ventilation is actually driving the decline, while Mask is offsetting some of that, whilst we, of course, have the ongoing effect of the Sleep remediation in the sleep devices part of the business.

Richard Felton: Great. Thanks very much.

Operator: Thank you. We will now go to our next question, and your next question comes from the line of David Adlington from JP Morgan. Please go ahead.

David Adlington (JP Morgan): Morning, guys. Thanks for the questions. Firstly, just on orders, you said you faced a tough comp, but I think it was only 1% last year and the year before that was down 15%. So I just wondered if you had some further call, it would be useful either by – notable weakness, either by product category or by region.

Secondly, just on your one-off charges, it looks like you've shifted 100 basis points from restructuring to other quality-related charges in Connected Care. I just wondered what the reason for that change was, please.

Abhijit Bhattacharya: Yeah. Hi David. Maybe let me answer the first question. I mentioned that there were tough comps in 2021 and 2022, so we had actually a 36% increase in comparable order intake in Diagnosis & Treatment in Q2 2021. And we followed that by another 2% increase last year. So, I think that's where the tough comps come, because it's already on a high order intake number, and you see that also in the IR deck. We have shown that on page 14.

The second thing is, of course, we mentioned earlier that it's lumpy, right, so Q1, we had strong growth – we had a double-digit growth in Q1, and, therefore, this lumpiness will continue. And that's why we say also that we have confidence in order intake growth in the second half of the year, because the funnel remains strong.

The one-off charges, sorry, I missed the second part of the question. The one-off charges is for what? Could you just repeat that, David, your second part of your question?

David Adlington: Yeah, your guidance on the one-off charges. 100 basis points seems to have shifted from restructuring. That's gone down by 100 basis points. But your quality-related charges with respect to Connected Care's gone up by 100 bps. So just wondered if we should read anything into that.

Abhijit Bhattacharya: Yeah, no, not really. It's – basically, as we have been going through the restructuring, we have found that there has been also some attrition, so that cost has gone down. And in the second half of the year, we are continuing with the remediation of the 483 that we had, so that is leading to some cost as well as legal costs related to Sleep and Respiratory. So again, overall the guidance remains the same, but it's just a shift in line.

David Adlington: Okay. And maybe just a cheeky follow-up, just into the foreign-exchange impact. I just wondered where you're expecting that to be at current rates for the rest of the year. Thanks.

Abhijit Bhattacharya: Yeah, look, typically, the way we manage our foreign exchange, it fluctuates between plus to minus 10-20 bps in a year. So, it should be within that range. It's not something big that we expect.

David Adlington: Thanks.

Operator: Thank you. We will now go to your next question, and your next question comes from the line of Robert Davies from Morgan Stanley. Please go ahead.

Robert Davies (Morgan Stanley): Yes. Thanks for taking my questions. My first one was just around the cash guide. I noticed there was no change in the free cash flow guidance for the year, even though you had some notable improvement year-on-year I think in the working capital metrics, January to June, and also the CAPEX was running low. So, I would just be, kind of, interested why you didn't revise the free cash flow guidance, even though the EBIT – sorry, the sales and margin guidance had been updated. That was my first question.

My second question is just on the trajectory of margins, I guess, in Personal Health. I'd just be curious what your thought process is there going into the back half-year. I noticed you

are obviously back in the positive growth territory, but the margins haven't really kind of kicked through. Is there a sort of level we should think about where margins could kick in? And I know there's quite a seasonal heavy 4Q trajectory there. I just wondered if there's anything to think about heading into the back half of this year that might change that.

And then the last one was just within the D&T business. Obviously, you had a few questions already about order trajectory. I'd just be curious in terms of modality of product within that business, if you're seeing anything to particularly call out as strong or weak in the quarter. Thank you.

Abhijit Bhattacharya: No. So, let me just – it's a good point on cash guidance. Look, we had given a range of \$0.7 billion to \$0.9 billion, which was, let's say, quite a broad range. We will have improvements in earnings, as you've seen. We have upped the guidance there to the higher end of the range. I expect that it will take a bit longer for us to get our inventories down as much as we would have liked this year, because, let's say, to get all the matching inventories and flow through to customers will probably take until the middle of next year. So again, we will probably be at the higher end of that guidance, but not at this stage to raise that guidance amount by a small amount. So we have confidence of being in the range. We have started well, and we will continue down that track.

Regarding margins in PH, we have already got into the – I think it was 100 basis points already in this quarter. Growth will continue in Q3 and Q4, so you should see also margin improvements coming in Q3 and Q4, so there's nothing that I would signal in terms of – yeah. Of course, given where we are in demand there, we are going to need to invest in advertising and promotion to, kind of, stimulate some demand to drive that growth, but not really much different.

Then your last question was on the order intake and in the modality.

Robert Davies: Yes.

Abhijit Bhattacharya: There's not really something significant to call out there. I think we – I think most of the lumpiness we see across the portfolio, so we had, let's say, good order intake across modalities in Q1 and we see, let's say, the mirror impact in Q2. And as we work down the backlog in MR, which currently is long, we hope to, let's say, start getting more and more order intake there, because currently, given the lead times, we are a bit hindered there. But there's not any specific modality which is, let's say, hugely different in terms of the pattern that we see.

Robert Davies: That's great. Thank you very much.

Operator: Thank you. We will now go to our next question, and your next question comes from the line of Graham Doyle from UBS. Please go ahead, your line is open.

Graham Doyle (UBS): Morning, guys. Thanks a lot for taking my questions. Just one on D&T, on the Consent Decree. The margin was obviously down sequentially – I mean, strong but down sequentially in D&T in Q2. I think at the start of the year, we were, kind of, still talking about relatively normal phasing in that. Typically, each quarter goes by, you generate more revenue, you generate a better margin. How should we think about Q3 and Q4? So when we think about that mix effect you flagged, Abhijit, how do we think about that going through the next couple of quarters?

And then just a, sort of, broader question on the Consent Decree, which isn't the specifics of timing. It's just when we think about the process, it's been going on for a year now. Is it – presumably, that is a, sort of, negotiation and there are things that you want that you are trying to push for and vice versa, but is it feasible that we just don't get an agreement on a Consent Decree? And what happens there? Thank you very much.

Abhijit Bhattacharya: Yeah. So, on D&T, I don't like – like I mentioned in the speech, right, there is a shift of phasing of cost as well as mix between Q1 and Q2. I would not read that too much as structural. Yes, we will have a stronger Q2 – second half in terms of margin in Diagnosis & Treatment, so I think if I remember, right, in 2020 – or 2019, we were at the 12.7. We will make a, kind of, good recovery towards that, so there will be strong improvement year-on-year. And again, between one quarter and the next, I would not read too much into it. We had also a higher mix, if I recall correctly, of Ultrasound in Q1, and a slightly stronger mix of DI[?] in Q2 that affects it a bit, and a certain phasing of service cost between Q1 and Q2. So, I would not read too much into that at this stage. We will continue improving as the year goes by.

Roy Jakobs: On the second one, maybe on the CD, so starting with your last part of the question, I think we will get to a Consent Decree, so that's just – it is a matter of time, so I don't think it's – there's no scenario that we will not get there, because it was initiated so it will be concluded. I think if you look at the timeline, actually, we are now, kind of, in a year after it started, but actually, if you look to a comparable own experience we had with the AD, which was of much smaller size and complexity, it also was over a year discussion to get to, kind of, a Consent Decree. So, I would not read also too much into the fact that we are now passing the one-year mark. And also if you look to other Consent Decree discussions with other parties, you will see that these timelines are not, kind of, out of the normal. This needs to be done diligently. And as we said before, yeah, this is a significant one, given that the Sleep and Respiratory recall was a sizeable affair.

So, I think that is what we are working through together and that's also what we will bring to conclusion at the right time.

Graham Doyle: Okay. Great. That's really clear. Thanks a lot, guys.

Operator: Thank you. So we'll now go to our next question, and your question comes from the line of Sezgi Oezener from HSBC. Please go ahead, your line is open.

Sezgi Oezener (HSBC): Hi. Thanks for taking my questions. Just two, please. First of all, on the change that you had, the transfer of Enterprise Informatics from D&T to CC, we can see how the margins of that business were so far. But going forward, can you give some colour on the projected outlook of that business in terms of growth and margins and what kind of market you're seeing there?

And second of all, on free cash flow, it was mentioned, of course, the fact that guidance remained the same despite higher guidance, and also even though the second quarter tends to be a lot stronger from a cash flow perspective. Was the fact that some of the liabilities[?] are not certain yet a factor in that? And do you see any downside risk to that guidance, given the first half free cash flow stood much lower? Thank you.

Roy Jakobs: So maybe let me take the first one. Indeed, I think we put Enterprise Informatics to Connected Care. I think the importance was that we really put it as a separate vertical, where we combined the different informatics assets actually to ensure that the capabilities to run that in an end-to-end manner actually yield its effect. And I can say that actually, we do see the impact coming into play. We have mentioned that the growth we expect should be double of what we grow at Philips, and also, we have seen strong growth in that. On order intake, we also said that, kind of, we would be a bit cautious, because we really want to fulfil well, and the delivery of these installations are important, so we are working hard on adequate delivery. And the margins are increasing. We have made certain choices for scaling the bigger platforms that we have, and that is yielding effect. And also, we expect with further growth acceleration that that will scale further.

So actually, we have seen the first impact, which was positive. There's a lot of momentum, as you can understand. There's a lot of demand for workflow improvement. AI is very hot and a big topic to see, kind of, how we can help the current customers with generative and analytical AI in their workflow and to drive patient outcomes. So we're also applying that. And we have multi-vendor solutions that actually can help across Imaging, Monitoring, and also in providing care across care settings. So, it is a part that actually is generating a lot of interest and we're having the dialogues with customers as we speak.

Abhijit Bhattacharya: Yeah. Sezgi, maybe to understand your question on cash flow, is it that because we have a stronger second half you are questioning the guidance, whether it should go up? I'm not very clear, sorry. Could you just ask that again?

Sezgi Oezener: Actually, the question is more like, do you see the risk to the current guidance, which was not updated, to the downside or upside, given that your second half tends to be much stronger, but you had a guidance upgrade in other metrics but not in free cash flow and first-half guidance – first-half actual free cash flow is – it shows significant improvement year-on-year, but compared to guidance it's on the weaker side?

Abhijit Bhattacharya: Yeah. I would not say that the first-half guidance is on the weaker side. If you look, typically, like you mentioned, our second-half cash flow is much stronger. We are actually pretty happy with where we are with the first half of the year. So I don't see any risk to the guidance. In fact, as I just mentioned, we will probably be at the upper end of the current guidance.

Sezgi Oezener: Okay. That's very helpful. Thanks a lot.

Operator: Thank you. As a reminder, if you would like to ask a question, please press the star followed by two times one on your telephone. We will now go to our next question, and your next question comes from the line of Falko Friedrichs from Deutsche Bank. Please go ahead.

Falko Friedrichs (Deutsche Bank): Thank you and good morning. I have two questions left, please, both on D&T. And the first one, on this mid-single-digit growth in Diagnostic Imaging, can you provide some kind of a split into MRI and CT?

And then secondly, what was driving this continued strong growth in your Ultrasound business? Thank you.

Abhijit Bhattacharya: Yeah, Falko, we provide a lot of colour. Now going into every modality and the specific becomes maybe even too much colour. But yes, across the board we have – we continue to grow. So, both the MRI and CT were actually nicely up and the growth in Ultrasound comes from the fact that the order book is very, very strong, and last year we had component issues in Ultrasound in Q3 and Q4. And once that is resolved, we are just going through the order book so that continues good momentum, and our shares are also trending well. So, I think overall, yeah, it's – you see growth across the board and Ultrasound is largely due to the order book that we were carrying.

Falko Friedrichs: Perfect, thank you.

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

Roy Jakobs: Thank you all for joining our call. As I said at the beginning, I'm pleased with the progress that we are making as we see that the measures that we have been taking at the beginning of the year are really yielding effect. And as a result, we delivered strong operational performance, with 9% comparable sales growth, improvement in profitability, operating cash flow. And that was coming from all businesses and all regions. We also expect to carry that into the second half, that positive momentum, based on further progress on the three priorities that we are executing against, and that actually led us to raise our guidance for the full year. So, whilst uncertainties, especially also in our environment, remain, we remain confident in our plan, the execution of it and will stay the course to, kind of, come back quarter-over-quarter, showing an improvement path for Philips on the long-term value creation trajectory.

So, thank you for listening in. Looking forward to connect with you and wish you a further great day.

Operator: Thank you. This concludes the Royal Philips Second Quarter and Semi-Annual 2023 Results Conference Call on Monday, 24th July 2023. Thank you for participating. You may now disconnect.

[END OF TRANSCRIPT]