

2 Our strategic focus

2.1 Addressing health challenges through innovation

All around the world, resource constraints are driving a shift to value-based healthcare – a system that aims to increase access to care and improve patient outcomes while also raising cost productivity. At the same time, aging populations and the rise of chronic diseases like heart disease and respiratory conditions are driving up demand for healthcare.

In parallel, a growing focus on healthy living and prevention means more and more people are looking for new ways to proactively monitor and manage their health, also in home and community settings. And the digitalization of healthcare has reached the point where value is shifting from stand-alone products to solutions combining systems, smart devices, software and services, which deliver greater benefits to customers.

Philips sees significant value in more integrated forms of healthcare, unlocking the power of data and artificial intelligence at the point of care, while at the same time optimizing care delivery across the health continuum. This includes putting increased emphasis on both primary and secondary prevention and population health management programs.

At Philips, we are striving to make the world healthier and more sustainable through innovation, with the goal of improving the lives of 3 billion people a year by 2025.

In today's increasingly connected world, the convergence of Philips' consumer technologies that facilitate healthy living, medical technologies that help clinicians to deliver better diagnosis and treatment, and cloud-based technologies that support data sharing and analysis, will be a key enabler of more effective, lower-cost integrated health solutions.

We like to visualize healthcare as a continuum since it suggests the notion of continuous care. And it becomes very compelling when one thinks of this continuum as being *connected*.

By addressing healthcare as a 'connected whole' in this way, we can unlock gains and efficiencies and drive innovations that help deliver on the 'quadruple aim': enhancing the patient experience, improving health outcomes, lowering the cost of care, and improving the work life of care providers.

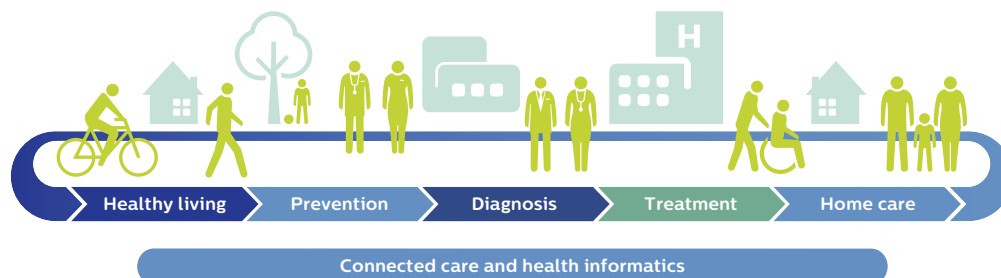
With our global reach, deep insights and leading innovations, we are uniquely positioned in 'the last yard' to consumers and care providers, delivering:

- connected products and services supporting the health and well-being of people
- integrated modalities and clinical informatics to deliver definitive diagnosis
- real-time guidance and smart devices for minimally invasive interventions
- connected therapeutic products and services for chronic care patients.

Underpinning these solutions, and spanning the health continuum, our connected care and health informatics solutions enable us to:

- connect patients and providers for more effective, coordinated, personalized care
- manage population health, leveraging real-time patient data and clinical analytics.

We are focusing on end-to-end pathways – at present primarily cardiology, oncology, respiratory care, and pregnancy and parenting – where we believe our integral approach can add even greater value for our customers.



More and more, we are teaming up with hospital and health systems to understand their needs, provide integrated solutions, and engage in multi-year cooperation to drive improvements in terms of patient outcomes, quality of care delivery and cost productivity.

In this context, we are pioneering new business models that fit our customers' needs better. These include Technology Managed Services, as well as Software as a Service and Product as a Service models. We have also started to take co-accountability for our customers' patient outcomes and productivity.

As we embark on the next phase of our health technology journey, the drivers below are designed to help deliver higher levels of customer value and quality, boost growth, deliver winning solutions, and improve our results:



2.2 How we create value

Meeting people's unmet needs

At Philips, value creation always starts with listening to people in local markets – consumers, doctors, nurses, hospital executives and administrators – so we understand the specific challenges they face in their day-to-day work.

This gives us a deep insight into their needs and aspirations. We then apply our innovative competencies, strong brand, global footprint and talented, engaged people – often in long-term partnerships – to deliver solutions that meet these needs, making the world healthier and more sustainable.

To measure the impact we are having around the world, we have developed our independently verified Lives Improved model. We take a two-dimensional approach – social and ecological – to improving people's lives. Products and solutions that directly support the curative (care) or preventive (well-being) side of people's health, determine the contribution to the social dimension. The contribution to the ecological dimension is determined by means of our Green Products and Solutions portfolio.

Our business system

With its four interlocking elements, the Philips Business System (PBS) is designed to help us deliver on our mission and vision – and to ensure that success is repeatable. As we execute our strategy and invest in the best opportunities, leverage our unique strengths and become operationally excellent, we will be able to consistently deliver value to our customers, consumers and other stakeholders.

- **Strategy – Where we invest:** We manage our businesses with clearly defined strategies to deliver solutions across the health continuum and allocate resources to maximize value creation.
- **Capabilities, Assets and Positions – Our unique strengths:** We strengthen and leverage our core Capabilities, Assets and Positions – our deep customer insights, technological innovation, global footprint, our people, and the trusted Philips brand – as they create differential value.
- **Excellence – How we operate:** We are a learning organization that applies common operating principles and practices to deliver to our customers with excellence.
- **Path to Value – What we deliver:** We define and execute business plans that deliver sustainable results along a credible Path to Value.

The 'Creating value for our stakeholders' diagram, based on the International Integrated Reporting Council framework, shows how – with the Philips Business System at the heart of our endeavors – we use six different forms of capital to drive value in the short, medium and long term. All numbers are for the year ended December 31, 2017.

Capital input

The capitals (resources and relationships) that Philips draws upon for its business activities

Human

- Employees **73,951, 120** nationalities, **36%** female
- Philips University **1,200** new courses, **830,000** hours, **570,000** training completions
- **27,997** employees in growth geographies
- New **Inclusion & Diversity** programs

Intellectual

- Invested in R&D **EUR 1.76 billion** (Green Innovation **EUR 233 million**)
- Employees in R&D **9,787** across the globe including growth markets

Financial

- Net debt **EUR 2.8 billion**
- Equity **EUR 12.0 billion**
- Market capitalization **EUR 29.2 billion**

Manufacturing

- Manufacturing sites **38**, cost of materials used **EUR 4.9 billion**
- Total assets **EUR 25.3 billion**
- Capital expenditure **EUR 420 million**

Natural

- Energy used in manufacturing **3,072 terajoules**
- Water used **888,000 m³**
- Recycled plastics in our products **1,850 tonnes**

Social

- Philips Foundation
- Stakeholder engagement
- New volunteering policy

**Value outcomes**

The result of the application of the capitals to Philips' business activities and processes as shaped by the Philips Business System

Human

- Employee Engagement Index **76%** positive
- Sales per employee **EUR 240,429**
- Employee benefit expenses **EUR 5,824 million**

Intellectual

- New patent filings **1,200**
- IP Royalties Adjusted EBITA **EUR 225 million**
- **165** design awards

Financial

- Comparable sales growth **4%**
- Adjusted EBITA¹⁾ as a % of sales **12.1%**
- Net cash provided by operating activities **EUR 1,870 million**
- Net capital expenditures **EUR 685 million**
- Dividend **EUR 742 million**
- Corporate taxes paid **EUR 349 million**
- **60%** Green Revenues

Manufacturing

- **EUR 17.8 billion** products and solutions sold, with **2.2 billion** Lives improved

Natural

- **11%** revenues from circular propositions
- Net CO₂ emissions **627 kilotonnes**
- **245,000 tonnes** (estimated) products put on the market
- **24.6 kilotonnes** waste, of which **80%** recycled
- Environmental impact Philips' operations **EUR 200 million**

Social

- Brand value **USD 11.5 billion**
- Partnerships with UNICEF, Red Cross and Ashoka

**Human**

We employ diverse and talented people and give them the skills and training they need to ensure their effectiveness and their personal development and employability.

**Intellectual**

We apply our innovation and design expertise to create new products and solutions that meet local customer needs.

**Financial**

We raise the funds we need from shareholders and other capital providers. We allocate this capital to the businesses and markets we think offer the best prospects for growth and returns.

**Manufacturing**

We apply Lean techniques to our manufacturing processes to produce high-quality products. We manage our supply chain in a responsible way.

**Natural**

We are a responsible company and aim to minimize the environmental impact of our supply chain, our operations, and also our products and solutions.

**Social**

We contribute to our customers and society through our products and solutions, our tax payments, the products and services we buy, and our investments in local communities.

¹⁾ Non-IFRS financial measure. For the definition and reconciliation to the most directly comparable IFRS measure, refer to [chapter 5, Reconciliation of non-IFRS information](#), of this Annual Report.

3 Group performance

“2017 was a year of solid progress, as we generated sales of EUR 17.8 billion underpinned by a 4% comparable sales growth, improved our operating profitability margin by 110 basis points, delivered a strong operating cash flow of EUR 1.9 billion, reduced our interest expenses by over EUR 100 million and increased net income from continuing operations to EUR 1,028 million.” **Abhijit Bhattacharya**, CFO Royal Philips

3.1 Financial performance

Management summary

- Sales rose to EUR 17.8 billion, a nominal increase of 2%, which reflected 3% nominal growth in the Personal Health businesses and Diagnosis & Treatment businesses and flat year-on-year sales in the Connected Care & Health Informatics businesses. On a comparable basis⁹⁾ the 4% growth was driven by 6% growth in the Personal Health businesses and 3% growth in the Connected Care & Health Informatics and Diagnosis & Treatment businesses.
- As of December 31, 2017, Philips' shareholding in Philips Lighting was decreased to 29.01% of Philips Lighting's issued share capital. As a result, Philips no longer has control over Philips Lighting and has ceased to consolidate Philips Lighting. With the completion of this transaction, Philips reached an important milestone in pivoting Philips into a focused health technology company. For further information, refer to [sub-section 3.1.1, Philips Lighting sell-down](#), of this Annual Report.
- Net income amounted to EUR 1.9 billion and increased by EUR 379 million compared to 2016, driven by improvements in operational performance, lower net financial expenses and higher discontinued operations results, partly offset by higher restructuring and acquisition-related charges and higher income taxes, which included a tax charge of EUR 171 million due to the US Tax Cuts and Jobs Act. Net income is not allocated to segments as certain income and expense line items are monitored on a centralized basis.
- Adjusted EBITA⁹⁾ totaled EUR 2.2 billion, or 12.1% of sales, an increase of EUR 232 million, or 110 basis points as a % of sales, compared to 2016. The productivity programs delivered annual savings of approximately EUR 483 million, ahead of the targeted savings of EUR 400 million, and included approximately EUR 260 million procurement savings, led by the Design for Excellence (DfX) program, and EUR 223 million savings from other productivity programs.
- Net cash provided by operating activities amounted to EUR 1.9 billion and increased by EUR 700 million compared to 2016. Free cash flow⁹⁾ amounted to EUR 1.2 billion and increased by EUR 756 million compared to 2016. The increase was mainly driven by higher earnings and the dividend related to the retained interest in the combined businesses of Lumileds and Automotive, lower outflows related to pension de-risking settlements, as well as the cash outflows in Q4 2016 of EUR 280 million related to the Masimo agreements. For further information on the Masimo agreements, refer to [note 19, Provisions](#).
- On June 28, 2017, Royal Philips announced a EUR 1.5 billion share buyback program. Philips started the program in the third quarter of 2017 and continues to make progress. As the program was initiated for capital reduction purposes, Philips intends to cancel all of the shares acquired under the program.
- In line with our mission to improve people's lives, we have embedded sustainability at the heart of our business processes, and Philips was named industry leader in the Dow Jones Sustainability Index for the 3rd year in a row. In the Carbon Disclosure Project, we achieved the highest score for the 5th year in a row. Green Revenues, including products and solutions sales, increased to 60% of total revenues in 2017.

⁹⁾ Non-IFRS financial measure. For the definition and reconciliation to the most directly comparable IFRS measure, refer to [chapter 5, Reconciliation of non-IFRS information](#), of this Annual Report.

Philips Group
Key data in millions of EUR unless otherwise stated
2015–2017

	2015	2016	2017
Sales	16,806	17,422	17,780
Nominal sales growth	16%	4%	2%
Comparable sales growth ¹⁾	4%	5%	4%
Income from operations	658	1,464	1,517
as a % of sales	3.9%	8.4%	8.5%
Financial expenses, net	(359)	(442)	(137)
Investments in associates	30	11	(4)
Income taxes	(169)	(203)	(349)
Income from continuing operations	160	831	1,028
Discontinued operations	479	660	843
Net income	638	1,491	1,870
Adjusted EBITA ¹⁾	1,688	1,921	2,153
as a % of sales	10.0%	11.0%	12.1%
Other indicators			
Net income attributable to shareholders per common share in EUR:			
basic	0.68	1.58	1.78
diluted	0.68	1.56	1.75
Net cash provided by operating activities	598	1,170	1,870
Net capital expenditures	(752)	(741)	(685)
Free cash flow ¹⁾	(154)	429	1,185

¹⁾ Non-IFRS financial measure. For the definition and reconciliation to the most directly comparable IFRS measure, refer to chapter 5, Reconciliation of non-IFRS information, of this Annual Report.

3.1.1 Philips Lighting sell-down

In September 2014, Philips announced its plan to sharpen its strategic focus by establishing two stand-alone companies focused on the HealthTech and Lighting opportunities respectively. To this end, a stand-alone structure was established for Philips Lighting within the Philips Group, effective February 1, 2016. Then, on May 27, 2016, Philips Lighting was listed and started trading on Euronext in Amsterdam under the symbol 'LIGHT'. Following the listing of Philips Lighting, Philips retained a 71.23% stake. The Initial Public Offering resulted in a net cash inflow of EUR 863 million and an increase of shareholders' equity of EUR 109 million.

In the course of 2017, Philips successfully completed three accelerated bookbuild offerings to institutional investors of a total of 65.35 million shares in Philips Lighting, gradually reducing Philips' stake in Philips Lighting's issued share capital to 29.01% by the end of 2017.

The first two transactions in February and April 2017, involving 48.25 million shares, resulted in a net cash inflow of EUR 1,065 million and had a positive impact on shareholders' equity of the Company of EUR 327 million. In April 2017, we concluded that a loss of control was highly probable due to further sell-downs of the remaining shares within one year. From that date Lighting was presented as a discontinued operation.

¹⁾ Non-IFRS financial measure. For the definition and reconciliation to the most directly comparable IFRS measure, refer to chapter 5, Reconciliation of non-IFRS information, of this Annual Report.

In November 2017, by selling another 17.1 million shares, Philips lost control, resulting in the deconsolidation of Philips Lighting. The sale of shares resulted in a net cash inflow of EUR 544 million and a gain of EUR 599 million recognized in Discontinued operations.

As of December 31, 2017, the retained interest in Philips Lighting represents a value of EUR 1,264 million. Philips will sell down its retained interest in Philips Lighting within one year and it is therefore presented under Assets classified as held for sale. The current position of 29.01% is a temporary position which fits in our overall single coordinated plan to sell Philips Lighting in its entirety. Consequently, any future results related to the retained interest – like value adjustments, results upon disposal and dividends – will be reflected in Discontinued operations.

Subsequent to deconsolidation, Philips recognized a valuation loss of EUR 104 million in discontinued operations related to the retained interest, reflecting the stock price developments of Philips Lighting until December 31, 2017.

3.1.2 Results of operations

Sales

The composition of sales growth in percentage terms in 2017, compared to 2016, is presented in the table below.

Philips Group
Sales growth composition in %
2017 versus 2016

	nominal growth	currency effects	consolidation changes	comparable growth ¹⁾
Personal Health	3.0	1.9	0.7	5.6
Diagnosis & Treatment	3.1	2.0	(1.6)	3.5
Connected Care & Health Informatics	0.2	1.9	1.1	3.2
HealthTech Other	(13.2)	0.2	0.1	(12.9)
Philips Group	2.1	1.9	(0.1)	3.9

¹⁾ Non-IFRS financial measure. For the definition and reconciliation to the most directly comparable IFRS measure, refer to chapter 5, Reconciliation of non-IFRS information, of this Annual Report.

Group sales amounted to EUR 17,780 million in 2017 and increased 2% on a nominal basis. Adjusted for a 1.8% negative currency effect and consolidation impact, comparable sales¹⁾ were 4% above 2016.

Our Personal Health businesses' sales amounted to EUR 7,310 million, which was EUR 211 million higher than in 2016, or 3% higher on a nominal basis and 6% higher on a comparable basis¹⁾. For further information, refer to sub-section 4.1.3, Financial performance, of this Annual Report.

Our Diagnosis & Treatment businesses' sales amounted to EUR 6,891 million, which was EUR 205 million higher than in 2016, or 3% higher on both a nominal and a comparable basis¹⁾. For further information, refer to [sub-section 4.2.3, Financial performance](#), of this Annual Report.

Our Connected Care & Health Informatics businesses' sales amounted to EUR 3,163 million, which was EUR 5 million higher than in 2016, flat year-on-year on a nominal basis and 3% higher on a comparable basis¹⁾. For further information, refer to [sub-section 4.3.3, Financial performance](#), of this Annual Report.

HealthTech Other reported sales of EUR 415 million, which was EUR 63 million lower than in 2016. For further information, refer to [sub-section 4.4.3, Financial performance](#), of this Annual Report.

Performance per geographic cluster

Philips Group
Sales by geographic cluster in millions of EUR
2015 – 2017

	'15	'16	'17	
	16,806	17,422	17,780	
	5,421	5,596	5,862	Growth geographies
	1,646	1,792	1,707	Other mature geographies
	6,063	6,279	6,409	North America
	3,675	3,756	3,802	Western Europe

Nominal sales growth by geographic cluster in % 2015 – 2017

	2015	2016	2017
Mature geographies ¹⁾	16.0	3.9	0.8
Growth geographies	15.3	3.2	4.8
Philips Group	15.8	3.7	2.1

¹⁾ Mature geographies include Western Europe, North America and Other mature geographies.

Comparable sales growth by geographic cluster¹⁾ in % 2015 – 2017

	2015	2016	2017
Mature geographies ²⁾	2.7	3.3	1.9
Growth geographies	8.1	8.4	8.0
Philips Group	4.4	4.9	3.9

¹⁾ Non-IFRS financial measure. For the definition and reconciliation to the most directly comparable IFRS measure, refer to [chapter 5, Reconciliation of non-IFRS information](#), of this Annual Report.

²⁾ Mature geographies include Western Europe, North America and Other mature geographies.

Sales in mature geographies were EUR 91 million higher than in 2016, or 1% higher on a nominal basis and 2% higher on a comparable basis¹⁾. Sales in Western Europe were 1% higher than in 2016 on a nominal basis and 3%

higher on a comparable basis¹⁾. Comparable sales in Western Europe reflected mid-single-digit growth in the Connected Care & Health Informatics businesses and Personal Health businesses, and flat year-on-year sales in the Diagnosis & Treatment businesses. Sales in North America increased by EUR 130 million, or 2% on a nominal basis and 3% on a comparable basis¹⁾.

Comparable sales in North America reflected mid-single-digit growth in the Connected Care & Health Informatics businesses and low-single-digit growth in the Personal Health businesses and Diagnosis & Treatment businesses. Sales in other mature geographies decreased by 5% on a nominal basis and by 2% on a comparable basis¹⁾. Comparable sales in other mature geographies showed low-single-digit growth in the Diagnosis & Treatment businesses, while the Connected Care & Health Informatics businesses and Personal Health businesses recorded a low-single-digit decline.

In growth geographies, sales were EUR 266 million higher than in 2016 and increased 5% on a nominal basis. The 8% increase on a comparable basis¹⁾ reflected double-digit growth in the Personal Health businesses, high-single-digit growth in the Diagnosis & Treatment businesses and low-single-digit growth in the Connected Care & Health Informatics businesses. The increase was driven by double-digit growth in Middle East & Turkey and high-single-digit growth in China, Latin America and Central & Eastern Europe.

Gross margin

In 2017, Philips' gross margin increased to EUR 8,181 million, or 46.0% of sales, from EUR 7,939 million, or 45.6% of sales, in 2016. Gross margin in 2017 included EUR 98 million of restructuring and acquisition-related charges, whereas 2016 included EUR 22 million of restructuring and acquisition-related charges. 2017 also included EUR 40 million of charges related to quality and regulatory actions, EUR 14 million of charges related to the consent decree focused on the defibrillator manufacturing in the US, and a EUR 36 million net release of provisions. Gross margin in 2016 also included a EUR 12 million net release of provisions and EUR 4 million of charges related to the separation of the Lighting business. The year-on-year increase was mainly driven by improved operational performance in the Personal Health, Diagnosis & Treatment and Connected Care & Health Informatics businesses, partly offset by higher restructuring and acquisition-related charges.

Selling expenses

Selling expenses amounted to EUR 4,398 million in 2017, or 24.7% of sales, compared to EUR 4,142 million, or 23.8% of sales, in 2016. Selling expenses in 2017 included EUR 127 million of restructuring and acquisition-related charges, compared to EUR 47 million in 2016. Selling expenses in 2017 also included EUR 9 million related to the separation of the Lighting

¹⁾ Non-IFRS financial measure. For the definition and reconciliation to the most directly comparable IFRS measure, refer to [chapter 5, Reconciliation of non-IFRS information](#), of this Annual Report.

business and EUR 4 million of charges related to the consent decree. Selling expenses in 2016 also included EUR 38 million related to the separation of the Lighting business.

General and administrative expenses

General and administrative expenses decreased to EUR 577 million, or 3.2% of sales, in 2017, compared to EUR 658 million, or 3.8% of sales, in 2016. 2017 included EUR 19 million of restructuring and acquisition related-charges, compared to EUR 5 million in 2016. General and administrative expenses in 2017 also included charges of EUR 21 million related to the separation of the Lighting business. 2016 also included charges of EUR 109 million related to the separation of the Lighting business, a EUR 26 million impairment of real estate assets, as well as a EUR 46 million gain from the settlement of a pension-related claim.

Research and development expenses

Research and development costs increased from EUR 1,669 million, or 9.6% of sales, in 2016 to EUR 1,764 million, or 9.9% of sales, in 2017. Research and development costs in 2017 included EUR 72 million of restructuring and acquisition-related charges, compared to EUR 21 million in 2016. 2017 also included charges of EUR 22 million related to portfolio rationalization measures, EUR 7 million of charges related to quality and regulatory actions, and EUR 2 million of charges related to the consent decree. The year-on-year increase was mainly due to higher restructuring and acquisition-related charges. Excluding these charges, research and development costs amount to 9.3% of sales.

Philips Group
Research and development expenses
in millions of EUR unless otherwise stated
2015 – 2017

	2015	2016	2017
Personal Health	383	412	415
Diagnosis & Treatment	596	629	715
Connected Care & Health Informatics	386	388	399
HealthTech Other	189	217	221
Legacy Items	8	23	14
Philips Group	1,562	1,669	1,764
as % of sales	9.3%	9.6%	9.9%

Net income, Income from operations (EBIT) and Adjusted EBITA⁹⁾

Net income is not allocated to segments as certain income and expense line items are monitored on a centralized basis, resulting in them being shown on a Philips Group level only.

The overview below shows sales, Income from operations and Adjusted EBITA⁹⁾ according to the 2017 segment classifications.

Philips Group
Sales, Income from operations and Adjusted EBITA⁹⁾
in millions of EUR unless otherwise stated
2016 – 2017

	Sales	Income from operations	%	Adjusted EBITA ⁹⁾	%
2017					
Personal Health	7,310	1,075	14.7%	1,221	16.7%
Diagnosis & Treatment	6,891	488	7.1%	716	10.4%
Connected Care & Health Informatics	3,163	206	6.5%	372	11.8%
HealthTech Other	415	(149)		(109)	
Legacy Items	1	(103)		(48)	
Philips Group	17,780	1,517	8.5%	2,153	12.1%

2016

Personal Health	7,099	953	13.4%	1,108	15.6%
Diagnosis & Treatment	6,686	546	8.2%	631	9.4%
Connected Care & Health Informatics	3,158	275	8.7%	324	10.3%
HealthTech Other	478	(129)		(66)	
Legacy Items	1	(181)		(76)	
Philips Group	17,422	1,464	8.4%	1,921	11.0%

⁹⁾ Non-IFRS financial measure. For the definition and reconciliation to the most directly comparable IFRS measure, refer to [chapter 5, Reconciliation of non-IFRS information](#), of this Annual Report.

Net income increased by EUR 379 million compared to 2016, driven by improvements in operational performance, lower net financial expenses and higher discontinued operations results, partly offset by higher restructuring and acquisition-related charges and higher income taxes, which included a total non-cash tax charge of EUR 171 million due to the US Tax Cuts and Jobs Act.

In 2017, Income from operations increased by EUR 53 million year-on-year to EUR 1,517 million, or 8.5% of sales. Restructuring and acquisition-related charges amounted to EUR 316 million, including the charges related to Spectranetics, compared to EUR 94 million in 2016. Income from operations in 2017 also included EUR 47 million of charges related to quality and regulatory actions, EUR 31 million of charges related to the separation of the Lighting business, EUR 26 million of provisions related to the CRT (Cathode Ray Tube) litigation in the US, EUR 22 million of charges related to portfolio rationalization measures, EUR 20 million of charges related to the consent decree focused on the defibrillator manufacturing in the US, a EUR 59 million net gain from the sale of real estate assets, and a EUR 36 million net release of provisions. 2016 also included EUR 152 million of charges related to the separation of the Lighting business, a EUR 26 million impairment of real estate assets, a EUR 12 million net release of provisions, and a EUR 46 million gain from the settlement of a pension-related claim.

⁹⁾ Non-IFRS financial measure. For the definition and reconciliation to the most directly comparable IFRS measure, refer to [chapter 5, Reconciliation of non-IFRS information](#), of this Annual Report.

Adjusted EBITA⁹⁾ amounted to EUR 2,153 million, or 12.1% of sales, and improved by EUR 232 million or 110 basis points as a % of sales compared to 2016. The improvement was mainly attributable to higher volumes, procurement savings and other cost productivity.

Personal Health businesses

In 2017, Income from operations amounted to EUR 1,075 million, or 14.7% of sales, an increase of EUR 122 million and a margin increase of 130 basis points compared to 2016. Adjusted EBITA⁹⁾ amounted to EUR 1,221 million, or 16.7% of sales, an increase of EUR 113 million or 110 basis points as a % of sales compared to 2016. For further information, refer to [sub-section 4.1.3, Financial performance](#), of this Annual Report.

Diagnosis & Treatment businesses

In 2017, Income from operations amounted to EUR 488 million, or 7.1% of sales, a decrease of EUR 58 million and a margin decrease of 110 basis points compared to 2016. Adjusted EBITA⁹⁾ amounted to EUR 716 million, or 10.4% of sales, an increase of EUR 85 million or 100 basis points as a % of sales year-on-year. For further information, refer to [sub-section 4.2.3, Financial performance](#), of this Annual Report.

Connected Care & Health Informatics businesses

In 2017, Income from operations totaled EUR 206 million, or 6.5% of sales, a decrease of EUR 69 million and a margin decrease of 220 basis points as a % of sales compared to 2016. Adjusted EBITA⁹⁾ totaled EUR 372 million, or 11.8% of sales, an increase of EUR 48 million or 150 basis points as a % of sales year-on-year. For further information, refer to [sub-section 4.3.3, Financial performance](#), of this Annual Report.

HealthTech Other

In HealthTech Other we report on the items Innovation, Emerging Businesses, IP Royalties, Central costs and Other.

In 2017, Income from operations amounted to a net cost of EUR 149 million, compared to a net cost of EUR 129 million in 2016. Adjusted EBITA⁹⁾ amounted to a net cost of EUR 109 million, compared to EUR 66 million in 2016. For further information, refer to [sub-section 4.4.3, Financial performance](#), of this Annual Report.

Legacy Items

Income from operations in 2017 amounted to a loss of EUR 103 million, and improved by EUR 78 million compared to 2016. For further information, refer to [sub-section 4.5.1, Financial performance](#), of this Annual Report.

Financial income and expenses

A breakdown of Financial income and expenses is presented in the following table.

Philips Group
Financial income and expenses in millions of EUR
2015 – 2017

	2015	2016	2017
Interest expense (net)	(300)	(299)	(182)
Sale of securities	20	3	1
Impairments	(46)	(24)	(2)
Other	(33)	(122)	46
Financial income and expenses	(359)	(442)	(137)

Net interest expense in 2017 was EUR 117 million lower than in 2016, mainly driven by lower interest expenses on net debt⁹⁾, as a result of the bond redemptions. Other financial income amounted to EUR 46 million in 2017, mainly due to dividend income related to the retained interest in the combined businesses of Lumileds and Automotive. For further information, refer to [note 7, Financial income and expenses](#).

Income taxes

Income taxes amounted to EUR 349 million, compared to EUR 203 million in 2016. The effective income tax rate in 2017 was 25.3%, compared to 19.9% in 2016. This increase was largely due to a tax charge of EUR 72 million for a valuation adjustment of Philips' US deferred tax assets following the enactment of the US Tax Cuts and Jobs Act in December 2017.

For 2018, we expect our effective tax rate to be within the range of 26%–28%, depending on the geographical mix of taxable income.

Investment in associates

Results related to investments in associates decreased from a gain of EUR 11 million in 2016 to a loss of EUR 4 million in 2017, mainly due to an impairment of EUR 4 million and lower share of income of associates in 2017 compared to 2016.

Discontinued operations

Discontinued operations consist primarily of the segment Lighting, the combined Lumileds and Automotive businesses, and certain divestments formerly reported as discontinued operations. The results related to these businesses are reported under Discontinued operations in the Consolidated statements of income and Consolidated statements of cash flows.

In 2017, Philips completed several transactions in Philips Lighting shares, which reduced the interest in this company from 71.23% as of December 31, 2016 to 29.01% as of December 31, 2017. In April 2017, triggered by a sale of Philips Lighting shares, we concluded that a loss of control was highly probable due to further sell-downs of the remaining shares within one year. From that date Lighting was presented as a discontinued operation. In November 2017 Philips lost control, resulting in the deconsolidation of Philips Lighting.

⁹⁾ Non-IFRS financial measure. For the definition and reconciliation to the most directly comparable IFRS measure, refer to [chapter 5, Reconciliation of non-IFRS information](#), of this Annual Report.

On June 30, 2017, Philips completed the sale of an 80.1% interest in the combined Lumileds and Automotive businesses to certain funds managed by affiliates of Apollo Global Management, LLC. The combined businesses of Lumileds and Automotive were reported as discontinued operations as from the end of November 2014.

Philips Group
Discontinued operations, net of income taxes
 in millions of EUR
 2015 – 2017

	2015	2016	2017
Lighting	247	244	896
The combined Lumileds and Automotive businesses	233	282	(29)
Other	(1)	134	(24)
Discontinued operations, net of income taxes	479	660	843

Net income of Discontinued operations

Discontinued operations results increased by EUR 183 million, mainly due to a EUR 599 million net gain from the deconsolidation of Philips Lighting, partly offset by a EUR 104 million charge related to the change in value of the retained interest in Philips Lighting, a tax charge of EUR 99 million due to the US Tax Cuts and Jobs Act, and the exclusion of the operational results of the combined businesses of Lumileds and Automotive from Discontinued operations following the divestment in Q2 2017. The year 2016 included the Funai arbitration award.

For further information, refer to [note 3, Discontinued operations and assets classified as held for sale](#).

Net income

Net income amounted to EUR 1,870 million, an increase of EUR 379 million compared to 2016, driven by improvements in operational performance, lower net financial expenses and higher discontinued operations results, partly offset by higher restructuring and acquisition-related charges and higher income taxes, which included a tax charge of EUR 171 million due to the US Tax Cuts and Jobs Act.

Basic earnings per common share from net income attributable to shareholders increased from EUR 1.58 per common share in 2016 to EUR 1.78 per common share in 2017.

Net income is not allocated to segments as certain income and expense line items are monitored on a centralized basis.

Non-controlling interests

Net income attributable to non-controlling interests increased from EUR 43 million in 2016 to EUR 214 million in 2017, mainly as a result of three sales transactions in Philips Lighting shares, which reduced the interest in this company from 71.23% as of

December 31, 2016 to 29.01% as of December 31, 2017. Philips Lighting was deconsolidated as from the end of November 2017.

3.1.3 Advertising and promotion

Philips' total advertising and promotion expenses were EUR 939 million in 2017, an increase of EUR 24 million compared to 2016. The total advertising and promotion investment as a percentage of sales was 5.3% in 2017 and was in line with 2016.

Philips' brand value increased by 2% to over USD 11.5 billion as measured by Interbrand. In the 2017 listing, Philips is ranked the 41st most valuable brand in the world.

3.1.4 Pensions

In 2017, the total costs of post-employment benefits amounted to EUR 69 million for defined-benefit plans and EUR 315 million for defined-contribution plans. These costs are reported in Income from operations except for the net interest cost component which is reported in Financial expense. The net interest cost for defined-benefit plans was EUR 37 million in 2017.

The overall funded status and balance sheet improved in 2017, mainly due to the transfer of Lighting to Discontinued operations and an additional contribution of EUR 219 million in the US.

2017 included a settlement of the Brazil pension plans leading to a decrease of the defined-benefit obligation of EUR 345 million and the recognition of a settlement loss of EUR 1 million.

In 2016, the total costs of post-employment benefits amounted to EUR 29 million for defined-benefit plans and EUR 299 million for defined-contribution plans. The net interest cost for defined-benefit plans was EUR 48 million in 2016.

2016 included a legal claim settlement gain of EUR 46 million related to the UK pension plan.

The overall funded status and balance sheet improved in 2016, mainly due to contributions of EUR 250 million in the US, partly offset by an increase of the defined-benefit obligation due to lower discount rates.

For further information, refer to [note 20, Post-employment benefits](#).

3.1.5 Restructuring and acquisition-related charges and goodwill impairment charges

Philips Group
Restructuring and related charges in millions of EUR
2015 – 2017

	2015	2016	2017
Restructuring and related charges per segment:			
Personal Health	38	16	8
Diagnosis & Treatment	25	6	63
Connected Care & Health Informatics	37	9	81
HealthTech Other	(20)	27	59
Legacy Items	1		
Philips Group	81	58	211
Cost breakdown of restructuring and related charges:			
Personnel lay-off costs	105	63	150
Release of provision	(55)	(34)	(37)
Restructuring-related asset impairment	26	14	77
Transfer to Assets held for sales			(5)
Other restructuring-related costs	5	14	27
Philips Group	81	58	211

In 2017, Income from operations included net restructuring charges totaling EUR 211 million. The most significant restructuring projects impacted the Connected Care & Health Informatics businesses, Diagnosis & Treatment businesses and HealthTech Other businesses and mainly took place in the Netherlands and the US. The restructuring comprised mainly product portfolio rationalization and the reorganization of global support functions.

In 2016, Income from operations included net charges totaling EUR 58 million for restructuring. The most significant restructuring projects were mainly related to overhead cost reduction programs in HealthTech Other and took place in the Netherlands.

For further information on restructuring, refer to [note 19, Provisions](#).

Philips Group
Acquisition-related charges in millions of EUR
2015 – 2017

	2015	2016	2017
Acquisition-related charges per segment:			
Personal Health	(1)		3
Diagnosis & Treatment	107	31	88
Connected Care & Health Informatics	1	4	10
HealthTech Other		1	5
Philips Group	107	37	106

In 2017, acquisition-related charges amounted to EUR 106 million. The Diagnosis & Treatment businesses recorded EUR 88 million of acquisition-related charges, mainly related to the acquisition of Spectranetics, a US-based global leader in vascular intervention and lead management solutions. Acquisition-related charges

relating to Volcano were also included as part of the Diagnosis & Treatment businesses' acquisition-related charges.

The 2016 acquisition-related charges amounted to EUR 37 million. The Diagnosis & Treatment businesses recorded EUR 31 million of acquisition-related charges, mainly related to Volcano.

In 2017, in addition to the annual goodwill-impairment tests for Philips, trigger-based impairment tests were performed during the year, resulting in a goodwill impairment of EUR 9 million.

In 2016, in addition to the annual goodwill-impairment tests for Philips, trigger-based impairment tests were performed during the year, resulting in a goodwill impairment of EUR 1 million.

For further information on goodwill sensitivity analysis, please refer to [note 11, Goodwill](#).

3.1.6 Acquisitions and divestments

Acquisitions

In 2017, Philips completed several acquisitions, with The Spectranetics Corporation (Spectranetics) being the largest. Spectranetics is a US-based global leader in vascular intervention and lead management solutions and is present in 11 countries. Acquisitions in 2017 and prior years led to acquisition and post-merger integration charges of EUR 88 million in the Diagnosis & Treatment businesses and EUR 10 million in the Connected Care & Health Informatics businesses.

In 2016, Philips completed two acquisitions, the largest being Wellcentive, a leading US-based provider of population health management software solutions. Acquisitions in 2016 and prior years led to acquisition and post-merger integration charges of EUR 31 million in the Diagnosis & Treatment businesses and EUR 4 million in the Connected Care & Health Informatics businesses.

Divestments

Apart from the sale of interest in Lumileds and Philips Lighting, Philips completed two divestments during 2017 for an aggregate cash consideration of EUR 54 million.

For details regarding the sale of interests in Lumileds and Philips Lighting, reference is made to [note 3, Discontinued operations and assets classified as held for sale](#) and [sub-section 3.1.1, Philips Lighting sell-down](#), of this Annual Report.

For details, please refer to [note 4, Acquisitions and divestments](#).

3.17 Changes in cash and cash equivalents, including cash flows

The movement in cash and cash equivalents for the years ended December 31, 2015, 2016 and 2017 are presented and explained below:

Condensed consolidated cash flow statements¹⁾ in millions of EUR 2015 – 2017

	2015	2016	2017
Beginning cash balance	1,873	1,766	2,334
Net cash provided by operating activities	598	1,170	1,870
Net capital expenditures	(752)	(741)	(685)
Free cash flows ²⁾	(154)	429	1,185
Acquisitions and divestments of businesses	(1,046)	(197)	(2,280)
Other cash flow from investing activities	(53)	(156)	(234)
Treasury share transactions	(425)	(526)	(414)
Change in debt	1,252	(1,611)	(205)
Dividend paid to shareholders of the Company	(298)	(330)	(384)
Sale of shares of Philips Lighting		825	1,060
Other cash flow items	80	(18)	(186)
Net cash flows from discontinued operations	537	2,151	1,063
Ending cash balance	1,766	2,334	1,939

¹⁾ Please refer to [section 11.7, Consolidated statements of cash flows](#), of this Annual Report.

²⁾ Non-IFRS financial measure. For the definition and reconciliation to the most directly comparable IFRS measure, refer to [chapter 5, Reconciliation of non-IFRS information](#), of this Annual Report.

Net cash provided by operating activities

Net cash provided by operating activities amounted to EUR 1,870 million in 2017, which was EUR 700 million higher than in 2016, mainly due to EUR 379 million higher earnings in 2017 and the higher outflows recorded in 2016 related to the Masimo agreements.

Net cash provided by operating activities amounted to EUR 1,170 million in 2016, which was EUR 572 million higher than in 2015, mainly due to EUR 853 million higher earnings and EUR 198 million net improvements in working capital-related inflows. Net cash provided by operating activities in 2015 included EUR 382 million cash outflows related to CRT litigation claims and higher pension de-risking settlements. 2016 also included EUR 280 million outflow related to the Masimo agreements (refer to [note 19, Provisions](#)) and a EUR 91 million premium payment related to the October 2016 bond redemption.

Net cash used for investing activities

In 2017, acquisitions of businesses (including acquisition of investments in associates) amounted to a cash outflow of EUR 2,344 million, which included the acquisition of Spectranetics for EUR 1.9 billion. Net cash proceeds from divestment of businesses amounted to EUR 64 million and were received mainly from divested businesses held for sale. Other investing activities mainly included EUR 295 million net cash used for foreign exchange derivative contracts related to

activities for funding and liquidity management, partly offset by EUR 90 million received related to TPV Technology Limited loans.

In 2016, acquisitions of businesses (including acquisition of investments in associates) amounted to a cash outflow of EUR 197 million, which included the acquisition of Wellcentive. Other investing activities mainly included EUR 128 million net cash used for foreign exchange derivative contracts related to activities for funding and liquidity management.

Net cash provided by (used for) financing activities

Net cash provided by financing activities in 2017 was EUR 55 million. Philips' shareholders were given EUR 742 million in the form of a dividend, of which the cash portion of the dividend amounted to EUR 384 million. Net cash proceeds of EUR 1,060 million related to the sales of shares in Philips Lighting. Change in net debt¹⁾ mainly reflected EUR 1.2 billion cash outflow related to the bond redemption and EUR 1 billion cash inflow from bonds issued. Additionally, net cash outflows for share buy-back and share delivery totaled EUR 414 million.

Net cash used for financing activities in 2016 was EUR 1,643 million. Philips' shareholders were given EUR 732 million in the form of a dividend, of which the cash portion of the dividend amounted to EUR 330 million. Net cash proceeds of EUR 825 million related to the sales of shares in Philips Lighting. Change in net debt¹⁾ mainly reflected the repayment of a loan related to the Volcano acquisition of EUR 1,186 million. Additionally, net cash outflows for share buy-back and share delivery totaled EUR 526 million.

Cash flows from discontinued operations

Discontinued operations cash flows in millions of EUR 2015 – 2017

	2015	2016	2017
Cash flows from operating activities	761	1,037	350
Cash flows from investing activities	(203)	(112)	856
Cash flows from financing activities	(20)	1,226	(144)
Total discontinued operations cash flows	537	2,151	1,063

In 2017, cash flows from operating activities reflect the period prior to the divestment of the combined Lumileds and Automotive business (six months of cash flows) and prior to the deconsolidation of Lighting (eleven months of cash flows). In 2017, cash flows from investing activities includes the net cash outflow related to the deconsolidation of Philips Lighting of EUR 175 million, consisting of EUR 545 million proceeds from the sale of shares on November 28, 2017, offset by the deconsolidation of EUR 720 million of cash and cash equivalents, and proceeds of EUR 1.1 billion received from the sale of the combined Lumileds and Automotive businesses.

¹⁾ Non-IFRS financial measure. For the definition and reconciliation to the most directly comparable IFRS measure, refer to [chapter 5, Reconciliation of non-IFRS information](#), of this Annual Report.

In 2016, cash flows from investing activities includes EUR 144 million cash inflow related to the Funai arbitration and cash flows from financing activities includes new funding of EUR 1.2 billion attracted by Philips Lighting.

3.1.8 Financing

Condensed consolidated balance sheets for the years 2015, 2016 and 2017 are presented below:

Philips Group
Condensed consolidated balance sheet¹⁾ in millions of EUR
2015 – 2017

	2015	2016	2017
Intangible assets	12,216	12,450	11,054
Property, plant and equipment	2,322	2,155	1,591
Inventories	3,463	3,392	2,353
Receivables	5,287	5,636	4,148
Assets held for sale	1,809	2,180	1,356
Other assets	4,080	4,123	2,874
Payables	(5,604)	(6,028)	(4,492)
Provisions	(4,243)	(3,606)	(2,059)
Liabilities directly associated with assets held for sale	(407)	(525)	(8)
Other liabilities	(3,204)	(3,052)	(2,017)
Net asset employed	15,719	16,725	14,799
Cash and cash equivalents	1,766	2,334	1,939
Debt	(5,760)	(5,606)	(4,715)
Net debt²⁾	(3,994)	(3,272)	(2,776)
Non-controlling interests	(118)	(907)	(24)
Shareholders' equity	(11,607)	(12,546)	(11,999)
Financing	(15,719)	(16,725)	(14,799)

¹⁾ Please refer to section 11.6, Consolidated balance sheets, of this Annual Report

²⁾ Non-IFRS financial measure. For the definition and reconciliation to the most directly comparable IFRS measure, refer to chapter 5, Reconciliation of non-IFRS information, of this Annual Report.

3.1.9 Debt position

Total debt outstanding at the end of 2017 was EUR 4,715 million, compared with EUR 5,606 million at the end of 2016.

Philips Group
Balance sheet changes in debt in millions of EUR
2015 – 2017

	2015	2016	2017
New borrowings/repayments short-term debt	(1,241)	1,319	4
New borrowings long-term debt	(94)	(1,304)	(1,115)
Repayments long-term debt	104	362	1,332
Forward contracts			(1,018)
Currency effects, consolidation changes and other	(425)	(223)	347
Transfer to liabilities directly associated with assets held for sale			1,342
Changes in debt	(1,656)	154	891

In 2017, total debt decreased by EUR 891 million compared to 2016. New borrowings of long-term debt of EUR 1,115 million were mainly due to the issuance of EUR 500 million floating-rate bonds due 2019 and EUR 500 million fixed-rate bonds due 2023. Repayments of long-term debt amounted to EUR 1,332 million, mainly

due to the early redemption of the 5.750% bonds due 2018 in the aggregate principal amount of USD 1,250 million. Payment obligations from forward contracts are mainly related to the EUR 1.5 billion share buyback program for capital reduction purposes announced on June 28, 2017 and are recorded as a financial liability under Long-term and Short-term debt. Other changes mainly resulting from consolidation and currency effects led to a decrease of EUR 347 million. EUR 1,342 million was transferred to Liabilities directly associated with assets held for sale, mainly Lighting debt.

In 2016, total debt decreased by EUR 154 million compared to 2015. New borrowings of EUR 1,304 million were mainly due to new loan facilities for Philips Lighting of EUR 740 million and USD 500 million to replace intragroup financing from Royal Philips. Repayments amounted to EUR 1,681 million, mainly due to the repayment of a USD 1,300 million bridge loan used for the Volcano acquisition, as well as the early redemption of USD 285 million in the aggregate principal amount of USD bonds. Other changes resulting from consolidation and currency effects led to an increase of EUR 223 million.

At the end of 2017, long-term debt as a proportion of the total debt stood at 86% with an average remaining term of 7.6 years, compared to 72% and 7.8 years at the end of 2016.

For further information, please refer to note 18, Debt.

3.1.10 Liquidity position

As of December 31, 2017, including the cash position (cash and cash equivalents), as well as its EUR 1 billion committed revolving credit facility, the Philips Group had access to available liquidity of EUR 2,939 million, versus Gross Debt (including short and long-term) of EUR 4,715 million.

As of December 31, 2016, including the cash position (cash and cash equivalents), as well as its then existing EUR 2.3 billion committed revolving credit facilities (including EUR 1.8 billion for Royal Philips and EUR 500 million for Philips Lighting), the Philips Group had access to available liquidity of EUR 4,634 million, versus Gross Debt (including short and long-term) of EUR 5,606 million.

Philips Group
Liquidity position in millions of EUR
2015 – 2017

	2015	2016	2017
Cash and cash equivalents	1,766	2,334	1,939
Committed revolving credit facilities/CP program/Bilateral loan	1,800	2,300	1,000
Liquidity	3,566	4,634	2,939
Available-for-sale financial assets at fair value	75	36	49
Short-term debt	(1,665)	(1,585)	(672)
Long-term debt	(4,095)	(4,021)	(4,044)
Net available liquidity resources	(2,119)	(936)	(1,728)

As at December 31, 2017, the reduction in net available liquidity resources compared to 2016 was mainly driven by the refinancing of the revolving credit facility and the transfer of the net liquidity of Philips Lighting (including cash and cash equivalents, short-term debt and long-term debt) into Discontinued operations.

Royal Philips has a EUR 1 billion committed revolving credit facility which was signed in April 2017 and will mature in April 2022. The facility can be used for general group purposes, such as a backstop of its Commercial Paper Programme.

The Commercial Paper Programme amounts to USD 2.5 billion, under which Royal Philips can issue commercial paper up to 364 days in tenor, both in the US and in Europe, in any major freely convertible currency. As of December 31, 2017, Royal Philips did not have any loans outstanding under these facilities.

Additionally, Philips held EUR 49 million of equity investments in available-for-sale financial assets (fair value at December 31, 2017). Refer to [note 13, Other financial assets](#). Furthermore, Philips is also a shareholder in Philips Lighting (EUR 1,264 million at year-end 2017) which is publicly listed and classified as asset held for sale.

Royal Philips' existing long-term debt is rated A- (with stable outlook) by Fitch, Baa1 (with stable outlook) by Moody's, and BBB+ (with stable outlook) by Standard & Poor's. Our net debt⁹⁾ position is managed in such a way that we seek to retain a strong investment grade credit rating. Furthermore, the Group's aim when managing the net debt⁹⁾ position is dividend stability and a pay-out ratio of 40% to 50% of continuing net income after adjustments. Royal Philips' outstanding long-term debt and credit facilities do not contain financial covenants. Adverse changes in the Company's ratings will not trigger automatic withdrawal of committed credit facilities nor any acceleration in the outstanding long-term debt (provided that the USD-denominated bonds contain a 'Change of Control Triggering Event' and the EUR-denominated bonds contain a 'Change of Control Put Event'). A description of Philips' credit facilities can be found in [note 18, Debt](#).

As at January 20, 2017, Philips early-redeemed the outstanding 5.750% bonds due 2018 having an aggregate principal amount of USD 1,250 million.

As at September 6, 2017, Philips successfully issued EUR 500 million floating-rate bonds due 2019 and EUR 500 million fixed-rate bonds due 2023. The net proceeds of the offering were used for the refinancing of the EUR 1 billion loan which was entered into for the purpose of financing the acquisition of Spectranetics and for general purposes.

Philips pools cash from subsidiaries to the extent legally and economically feasible. Cash not pooled remains available for local operational or investment needs. The company also faces cross-border foreign exchange controls and/or other legal restrictions in a few countries which could limit its ability to make these balances available on short notice for general use by the group.

Philips believes its current liquidity and direct access to capital markets is sufficient to meet its present financing requirements.

3.1.11 Shareholders' equity

Shareholders' equity decreased by EUR 547 million in 2017 to EUR 11,999 million at December 31, 2017. The decrease was mainly due to the negative impact of currency translation differences of EUR 984 million, share repurchases made in the open market over the course of the year, the purchase of forward contracts of EUR 1,079 million, and dividend payments to shareholders of Koninklijke Philips N.V. of EUR 384 million (including tax and service charges). This was mainly offset by net results of EUR 1,870 million and the sale of Philips Lighting shares of EUR 327 million.

The number of outstanding common shares of Royal Philips at December 31, 2017 was 926 million (2016: 922 million). At the end of 2017, the Company held 14.7 million shares in treasury to cover the future delivery of shares (2016: 7.2 million shares). This was in connection with the 20.8 million rights outstanding at the end of 2017 (2016: 33.5 million rights) under the Company's long-term incentive plans. At the end of 2017, the Company held 4.6 million shares for cancellation (2016: 0 shares). In 2016, Philips purchased call options on Philips shares to hedge the majority of the options granted to employees until 2013. As of December 31, 2017 Philips held 6.3 million call options as a hedge of 6.8 million remaining options granted to employees. In order to hedge share buy-back commitments, Philips also entered into several forward contracts in 2017. The total of forward contracts amounted to EUR 1.1 billion in 2017, of which EUR 60 million matured in 2017.

3.1.12 Cash obligations

Contractual cash obligations

The table below presents a summary of the Group's fixed contractual cash obligations and commitments at December 31, 2017. These amounts are an estimate of future payments, which could change as a result of various factors such as a change in interest rates, contractual provisions, as well as changes in our business strategy and needs. Therefore, the actual payments made in future periods may vary from those presented in the table below:

⁹⁾ Non-IFRS financial measure. For the definition and reconciliation to the most directly comparable IFRS measure, refer to [chapter 5, Reconciliation of non-IFRS information](#), of this Annual Report.

Philips Group
Contractual cash obligations^{1,2} in millions of EUR
 2017

	Payments due by period				
	total	less than 1 year	1-3 years	3-5 years	after 5 years
Long-term debt ³⁾	4,314	465	1,170	878	1,801
Finance lease obligations	306	93	131	53	29
Short-term debt	120	120			
Operating leases	741	172	226	147	196
Derivative liabilities	370	167	109		95
Interest on debt	1,785	132	252	226	1,175
Purchase obligations ⁴⁾	480	145	217	86	31
Trade and other payables	2,090	2,090			
Contractual cash obligations	10,205	3,383	2,105	1,389	3,328

¹⁾ Obligations in this table are undiscounted

²⁾ This table excludes pension contribution commitments and income tax liabilities in respect of tax risks because it is not possible to make a reasonably reliable estimate of the actual period of cash settlement

³⁾ Long-term debt includes short-term portion of long-term debt and excludes finance lease obligations

⁴⁾ Purchase obligations are agreements to purchase goods or services that are enforceable and legally binding for the Group. They specify all significant terms, including fixed or minimum quantities to be purchased, fixed, minimum or variable price provisions and the approximate timing of the transaction. They do not include open purchase orders or other commitments which do not specify all significant terms.

Philips has no material commitments for capital expenditures.

Certain Philips suppliers factor their trade receivables from Philips with third parties through supplier finance arrangements. At December 31, 2017 approximately EUR 286 million of the Philips accounts payable were known to have been sold onward under such arrangements whereby Philips confirms invoices. Philips continues to recognize these liabilities as trade payables and will settle the liabilities in line with the original payment terms of the related invoices.

Other cash commitments

The Company and its subsidiaries sponsor post-employment benefit plans in many countries in accordance with legal requirements, customs and the local situation in the countries involved. For a discussion of the plans and expected cash outflows, please refer to [note 20, Post-employment benefits](#).

The Company had EUR 112 million restructuring-related provisions by the end of 2017, of which EUR 87 million is expected to result in cash outflows in 2018. Refer to [note 19, Provisions](#) for details of restructuring provisions.

A proposal will be submitted to the upcoming Annual General Meeting of Shareholders to declare a dividend of EUR 0.80 per common share (up to EUR 750 million

if all shareholders would elect cash), in cash or shares at the option of the shareholder, against the net income for 2017. Further details will be given in the agenda for the Annual General Meeting of Shareholders, to be held on May 3, 2018.

Guarantees

Philips' policy is to provide guarantees and other letters of support only in writing. Philips does not provide other forms of support. The total fair value of guarantees recognized on the balance sheet amounts to EUR nil million for both 2016 and 2017. Remaining off-balance-sheet business and credit-related guarantees provided on behalf of third parties and associates decreased by EUR 11 million during 2017 to EUR 17 million (December 31, 2016: EUR 28 million).

3.1.13 Procurement

In spite of a challenging market environment, Philips came through with the 2017 procurement performance commitment. These results were driven by optimizing costs via various programs, including many DfX events, Total Cost of Ownership (TCO) programs and negotiations to secure the best possible outcome and overcome market headwinds.

Global growth is strengthening but the longer-term challenges remain. Policy stimulus supported the upturn, but the private investment recovery was modest. Continued reliance on credit to fund growth is heightening the risk of an eventual adjustment in China. In addition, a further shift toward protectionist policies in the US and a growing trend in Europe is a distinct threat. The currency risk remains in 2018 as the euro appreciated strongly against the US dollar and Chinese renminbi in 2017. Geopolitical tensions, terrorism and the European challenge with refugees could also play a key role in the outlook in several economies.

The higher commodity market prices over the last year created a challenging environment for Philips. The situation in 2018 will remain the same or will be more challenging, judging by the continuation of the economic improvement, speculation on further pick-up in commodity demand, and actual material market price increases over 2017. The low price levels of raw materials and energy during the period 2015–2016 have led to reduced investment in future supply. This creates the risk of new headwinds once real consumption picks up significantly again and the supply-demand situation reverses.

3.1.14 Real estate

Philips is present in more than 75 countries globally and has its corporate headquarters located in Amsterdam, the Netherlands. In 2017, we further increased the efficiency of our global Real Estate footprint by reducing the space provision by approximately 8%. Our real estate sites are spread across the globe, with key manufacturing and R&D sites in the Americas, Asia and Europe. As our company is very dynamic in streamlining and developing its business portfolio, the real estate

activities go hand-in-hand with that. In 2017, we made several adjustments to our footprint in the US (i.e. Foster City Pittsburgh, Nashville Tennessee, and Cambridge Massachusetts), but also in India (i.e. Chennai, Bangalore) and China (i.e. Shanghai), to optimize our global business solutions. We also rightsized and upgraded our Paris and Warsaw offices in EMEA and started to build our global business solutions in India, Poland and the United States. To attract new R&D talent we grew locations in Foster City, Bangalore, Pittsburgh, Moscow and others. With all these adjustments we have established a better balanced real estate footprint globally, which also enables our businesses to be close to their customer base. The vast majority of our locations consist of leased property, and we manage these closely to keep the overall vacancy rates of our property below 3% and to ensure that the right level of space efficiency and flexibility is in place to follow our business developments. The net book value of our land and buildings as at December 31, 2017, represented EUR 584 million, and construction in progress represented EUR 31 million. Our current facilities are in generally good operating condition and are adequate to meet the requirements of our present and foreseeable future operations.

3.1.15 Analysis of 2016 compared to 2015

The analysis of the 2016 financial results compared to 2015, and the discussion of the critical accounting policies, have not been included in this Annual Report. These sections are included in Philips' Form 20-F for the financial year 2017, which will be filed electronically with the US Securities and Exchange Commission.

3.2 Social performance

We are a purpose-driven company, aiming to improve the lives of 3 billion people annually by 2025. Our people find this purpose powerful, drawing inspiration from the societal impact we achieve. We have a highly engaged and committed workforce; our employee engagement score is consistently above the high-performing norm of 69%, rising from 71% in 2015, to 76% this year.

Our people strategy supports a constantly evolving workforce, capable of delivering strong business performance and executing our strategy. As such we focus on our Workforce of the Future, and our deep commitment to Inclusion and Diversity across our workforce, supported by a Culture of Performance. The future will require a new type of networked organization, where teams dynamically draw from across the organization and unite around a common purpose.

3.2.1 Improving people's lives

At Philips, we strive to make the world healthier and more sustainable through innovation. Our goal is to improve the lives of 3 billion people a year by 2025. To

guide our efforts and measure our progress, we take a two-dimensional approach – social and ecological – to improving people's lives. Solutions from our portfolio that directly support the curative or preventive side of people's health determine the contribution to the social dimension. This is also our contribution to the UN Sustainable Development Goal 3 ("to ensure healthy lives and promote well-being for all at all ages"). As healthy ecosystems are also needed for people to live a healthy life, the contribution to the ecological dimension is determined by means of our steadily growing Green Solutions portfolio, such as our energy efficient products in our Personal Health businesses. This is our contribution to Sustainable Development Goal 12 ("to ensure sustainable consumption and production patterns").

Through Philips products and solutions that support people's health, we improved the lives of 1.34 billion people in 2017 (2016: 1.22 billion), driven by all segments. Our Green Solutions (including Philips Lighting) that contribute to a healthy ecosystem contributed 1.86 billion lives. After the elimination of double counts – people touched multiple times – we arrived at 2.2 billion lives. This is an increase of around 100 million compared to 2016, driven by all segments, mainly in China, India, and North America.

In 2014, Philips pledged to support the United Nation's **Every Woman Every Child** initiative, committing to improve the lives of at least 100 million women and children in Africa and South East Asia by 2025. At the United Nations General Assembly week in September 2017, Philips made an extended commitment to improve the lives of 300 million people in underserved healthcare communities by 2025. Philips thereby recognized the often critical needs of women and children in many communities, but also the added burden arising from the increase in non-communicable diseases (NCDs) in communities already struggling without adequate access to healthcare. To monitor our progress on the extended commitment, we use the same Lives Improved methodology and in 2017 we improved the lives of 153 million people in underserved markets (an increase of 16 million compared to 2016).

More information on this metric can be found in [Methodology for calculating Lives Improved](#).

Lives Improved per market

To find out about our Lives Improved metric at global, regional and market level, go to <https://www.results.philips.com/#/interactive-worldmap>

The following table shows the Lives Improved metric per market.

Philips Group

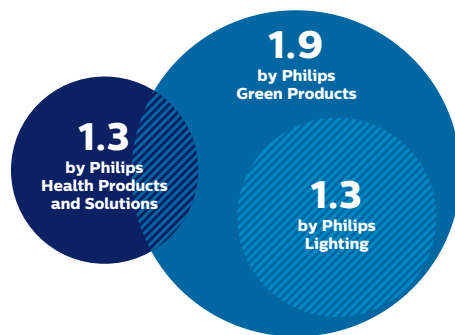
Lives Improved per market

Market	Lives Improved (million) ^{1,2)}	Population (million) ³⁾	GDP (USD billion) ⁴⁾
Africa	54	1,210	2,353
ASEAN and the Pacific	246	961	6,213
Benelux	29	29	1,380
Central & East Europe	96	167	1,616
Germany, Austria and Switzerland	94	100	4,749
France	59	66	2,605
Greater China	477	1,422	12,852
Iberia	46	57	1,524
Indian subcontinent	216	1,531	2,799
Italy, Israel and Greece	55	82	2,508
Japan	38	127	4,884
Latin America	177	636	5,693
Middle East & Turkey	110	358	3,120
Nordics	26	27	1,541
North America	358	362	21,003
Russia and Central Asia	67	244	1,880
UK & Ireland	51	71	2,905

¹⁾ Source: Philips, double counts eliminated²⁾ Includes Philips Lighting³⁾ Source: The World Bank, CIA Factbook & Wikipedia⁴⁾ Source: IMF, CIA Factbook & Wikipedia

Philips Group

Lives Improved in billions (includes Philips Lighting)

**Total: 2.2 billion (double counts eliminated)**

■ Double counts

*Conceptual drawing, areas do not reflect actual proportions***3.2.2 Workforce of the Future**

Changing workforce demographics, the dynamic business environment and limited availability of strategic skill sets mean that we need to focus on building strategic capabilities that we can offer through location and work arrangements. In 2017 we deepened our Strategic workforce planning practices across our businesses, geographies, and functions and continue to expand on our strategic people's practices, alongside business strategy and financials.

In Q3 2017 we addressed holistic workforce management, bringing all contingent workers under the responsibility of the HR function and recognizing the significant contribution of the skills and competencies that contingent workers offer. In 2018 we will further

manage workforce demand holistically through workforce modelling and talent intelligence, covering 100% of our workforce.

3.2.3 Inclusion & Diversity

At Philips, we believe that our workforce should be a reflection of the society in which we operate, a reflection of our customers, and the markets we serve.

We value our full workforce in all aspects of diversity, whether generational, gender, experience, ethnicity, race, sexual orientation, ability, nationality, or other aspects, and believe that an inclusive culture invites a full spectrum of ideas, opinions, and experiences into the decision making.

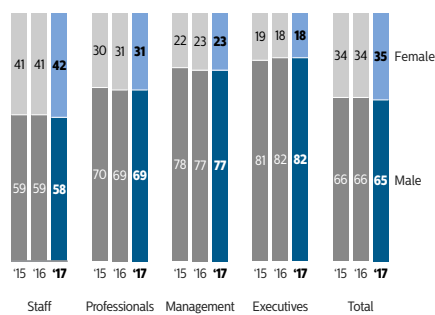
We believe in fairness, that all individuals have the opportunity to be successful, to be heard and to be valued, without prejudice, and we will strive for this to be felt across Philips. We believe that an inclusive culture and diverse workforce correlates to high performance, and therefore consider improvements in Inclusion & Diversity as a key opportunity for sustainable improvements in business performance.

Fostering Inclusion & Diversity will bring deeper customer insight from a place of understanding, which enables faster and more targeted responses to market changes, ultimately contributing to our collective ability to work together to deliver improved value to our customers.

In 2017 we set a renewed and enhanced intention for Inclusion & Diversity with a number of activations; we set a target for 25% gender diversity of senior leadership by 2020 and provided dashboards for our HR leaders to be able to track diversity for their organizations. We partnered with a leading Inclusion & Diversity training

provider to develop unconscious bias training, which will be delivered to our full workforce in 2018. We agreed principles of transparency for appointment and promotion opportunities, whereby we will transparently share open positions, and aim for diverse candidate slates and diverse interview panels for the recruitment of all senior leadership positions. We enhanced our existing Inclusion & Diversity leadership offerings, increasing instances of our Senior Women's Leadership Program and piloted a Women's Leadership program focused toward emerging professionals. We also revitalized our existing employee resource groups and launched an Executive Inclusion and Diversity Committee.

Philips Group
Gender diversity in %
2015 – 2017



Data insights

- 120+ nationalities bringing a rich diversity of capabilities, opinions and perspectives
- Gender diversity figures remained stable at 36% overall, with slight increases in the Staff, Professional and Management categories. Diversity of Executives dipped slightly from 19% to 18% female executives

I&D awards

We are delighted to be recognized externally for our inclusive culture externally. This year we achieved three awards in relation to our Life is better when #youareyou campaign, winning 'Best media representation' in Workday pride 2017, a Silver award in the category of 'society' at the SponsoRing awards, and a silver in the 'integration award' for identifying and engaging influencers in the WOMMA awards.

3.2.4 Culture of Performance

We have made strong progress in increasing performance. However to succeed as the leading health technology company, we need to further improve how we work and step up all aspects of performance. Our strategy requires us to work together to deliver compelling solutions across the health continuum that bring true value to consumers and customers. Our current behaviors include; winning, taking ownership, teamwork and acting with integrity, yet we can sharpen our focus on customers, delivering with quality, acting fast, and being eager to improve.

Living our desired Philips culture is foundational to succeeding in delivering on our vision, and to being the best company in health technology for people who share our passion.

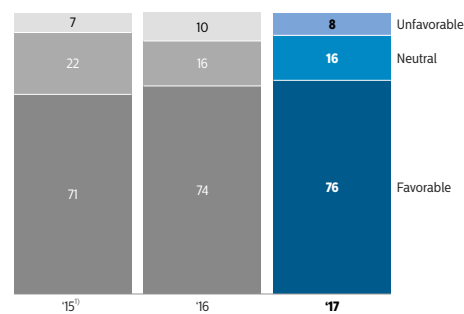
We recognize and value inspiring and inclusive leaders, through smart assessment, development planning, leadership programs, and coaching and sponsoring our talent. In 2017, 87% of Executive-level appointments were internal. We expect to continue to see a low percentage of external hiring at Executive level, where we will increasingly aim to develop and promote our talent from within, complemented with targeted external hiring for critical competencies.

Realizing a culture of performance is grounded in proper people management practices, high quality feedback, transparency and acting on performance and talent outcomes. We will increase our focus on individuals being able to drive their own career, supporting our employees with automation and Artificial Intelligence. We will ensure transparency of opportunities, and fair and open HR processes.

3.2.5 Employee engagement

High employee engagement is foundational to achieving our Philips health technology strategy. Our employee survey consistently reports high levels of employee engagement above the high performing norm of 69%, rising from 71% favorable in 2015 to 76% in 2017.

Philips Group
Employee Engagement Index in %
2015 – 2017



¹⁾ 2015 includes Philips Lighting

At Philips, we care for our people and believe that we are at our best when our team are at theirs. We understand work is only one part of life. That is why we offer a variety of innovative benefits and health programs to help keep our people mentally and physically strong, and foster flexibility to manage life's unexpected moments. We also continue to improve the employee journey, experience and value proposition, from attraction, through employment, development and progression, through to alumni. In 2017 we focused

on improving candidate experience and onboarding experience, receiving a Glassdoor interview experience award.

Our quarterly employee survey supports us in keeping our finger on the pulse of employee sentiment toward the company, listening to employees' ideas for improvement, demonstrating to employees that their feedback is valued, and working to ensure that every member of our global team has a role in creating lasting value for our customers, shareholders, and other stakeholders.

3.2.6 Employment

In 2017, we built out our health technology portfolio with acquisitions in key areas including image-guided therapy, healthcare consultancy, population health management, digital pathology, and sleep and respiratory care, growing our employee base by a further 1,798.

The total number of Philips Group employees (continuing operations) was 73,951 at the end of 2017, compared to 70,968 at the end of 2016, an increase of 2,983 employees. Following the sale of Lighting, Diagnosis & Treatment is now our largest employee segment with 35%, Personal Health at 31%, Connected Care & Health Informatics at 15% and 19% in HealthTech Other.

Philips Group
Employees per segment in FTEs at year-end
2015 – 2017

	2015	2016	2017
Personal Health	21,384	22,530	23,170
Diagnosis & Treatment	23,638	23,791	25,757
Connected Care & Health Informatics	10,290	11,033	10,949
HealthTech Other	11,493	13,570	13,965
Legacy Items		43	109
Continuing operations	66,805	70,968	73,951
Discontinued operations	46,154	43,764	
Philips Group	112,959	114,731	73,951

Philips Group
Employment in FTEs

	2015	2016	2017
Balance as of January 1	113,678	112,959	114,731
Consolidation changes:			
Acquisitions	1,865	163	1,812
Divestments	(300)	(571)	(332)
Changes in Discontinued operations	442	753	(43763)
Other changes	(2,726)	1,427	1,502
Balance as of December 31	112,959	114,731	73,951

Further to net growth from acquisitions and divestments, we increased our employee base by 1,480 employees, driven by a 6% increase in comparable sales growth (CSG)⁹ in our Personal Health businesses,

an increased focus on Quality & Regulatory, and the transition period to our future Global Business Services operating model.

Geographic footprint

Approximately 62% of the Philips workforce are located in mature geographies and 38% in growth geographies. In 2017, the number of employees in mature geographies increased by 1,774, mainly due to the acquisitions of Spectranetics and others. The number of employees in growth geographies increased by 1,209, driven mainly by the Personal Health sales growth and Global Business Services program.

Philips Group
Employees per geographic cluster in FTEs at year-end
2015 – 2017

	2015	2016	2017
Western Europe	21,569	20,657	21,055
North America	19,151	19,828	20,937
Other mature geographies	3,592	3,695	3,962
Mature geographies	44,311	44,180	45,954
Growth geographies	22,494	26,788	27,997
Continuing operations	66,805	70,968	73,951
Discontinued operations	46,154	43,764	
Philips Group	112,959	114,731	73,951

Employee turnover

In 2017, employee turnover amounted to 13.6% (of which 8.2% was voluntary) compared to 16.0% (9.6% voluntary) in 2016. The lower turnover in 2017 reflects the increasing employee engagement and strength of our health technology strategy.

Philips Group
Employee turnover in %
2017

	Staff	Professionals	Management	Executives	Total
Female	19.2	11.3	10.9	21.4	15.0
Male	19.2	9.5	9.3	15.8	12.8
Philips Group	19.2	10.1	9.7	16.8	13.6

Philips Group
Voluntary turnover in %
2017

	Staff	Professionals	Management	Executives	Total
Female	11.0	7.7	6.4	12.9	9.2
Male	11.5	5.9	4.4	5.2	7.7
Philips Group	11.3	6.5	4.9	6.6	8.2

3.2.7 Human Rights

We believe that businesses have the responsibility to respect Human Rights and the ability to contribute to positive Human Rights impacts. This is an area of growing importance to our employees, investors, customers, the communities where we operate and civil society groups. There is therefore both a business case and a moral requirement for ensuring that Human Rights are upheld across our own operations and our value chain.

⁹ Non-IFRS financial measure. For the definition and reconciliation to the most directly comparable IFRS measure, refer to chapter 5, Reconciliation of non-IFRS information, of this Annual Report.

Our General Business Principles (GBP) express our support and respect for Human Rights. In addition, we have employment-related policies that further reference and protect the rights of our people. In 2017, we developed an overarching [Human Rights policy](#) that aligns our different Human Rights-related policies towards a single goal: embed the responsibility to respect Human Rights through all our businesses, markets and functions. Philips' Human Rights policy ratifies Philips' commitment not to infringe people's rights and to address any adverse Human Rights impacts that we might cause. To that end, our policy states that we intend to conduct regular Human Rights impact assessments as part of an overall Human Rights due diligence process, and to remediate any negative Human Rights impacts. We are also firmly committed to continuous improvement: we will track and publicly report on progress (on an annual basis) as input to our dialogues with our internal and external stakeholders who are, or could potentially be, affected by our actions.

3.2.8 General Business Principles

The Philips General Business Principles (GBP) incorporate and represent the fundamental principles by which all Philips businesses and employees around the globe must abide. They set the minimum standard for business conduct, both for individual employees and for the company and our subsidiaries. Our GBP also serve as a reference for the business conduct we expect from our business partners and suppliers. Translations of the GBP text are available in 32 languages, allowing almost every employee to read the GBP in their native language. Detailed underlying policies, manuals, training, and tools are in place to give employees practical guidance on how to apply and uphold the GBP in their daily work environments. Details can be found at: www.philips.com/gbp.

In 2017, a total of 382 concerns were reported via the Philips Ethics Line and through our network of GBP Compliance Officers. The previous reporting period (2016) saw a total of 339 concerns, resulting in an increase of 13% in the number of reports.

This is a continuation of the upward trend reported since 2014, the year in which Philips updated its General Business Principles and deployed a strengthened global communication campaign. We believe this trend continues to be in line with our multi-year efforts to encourage our employees to speak up.

More information on the Philips GBP can be found in [chapter 6, Risk management](#), of this Annual Report. The results of the monitoring measures in place are given in [sub-section 13.3.6, General Business Principles](#), of this Annual Report.

3.2.9 Health and Safety

At Philips, we strive for an injury-free and illness-free work environment, with a focus on reducing the number of injuries and improving processes. As of 2016, the

Total Recordable Cases (TRC) rate is defined as a Key Performance Indicator (KPI), on which we set yearly targets for the company, Business Groups and industrial sites. For data comparability reasons, we also provide the Lost Workday Injury Cases (LWIC) rate.

We recorded 234 TRCs in 2017, a small decrease compared to 239 in 2016. These are cases where an injured employee is unable to work for one or more days, had medical treatment, or sustained an industrial illness. We will continue to monitor this KPI and actively set reduction targets for all our businesses in 2018.

In 2017, we recorded 113 LWICs. These are occupational injury cases where an injured person is unable to work for one or more days after the injury. This represents a 10% increase compared with 103 in 2016. The LWIC rate increased to 0.17 per 100 FTEs in 2017, compared with 0.16 in 2016. The number of Lost Workdays caused by injuries increased by 965 days (30%) to 4,170 days in 2017, mainly caused by longer recovery periods related to a limited number of incidents.

For more information on Health and Safety, please refer to [sub-section 13.3.7, Health and Safety performance](#), of this Annual Report.

3.2.10 Working with stakeholders

In organizing ourselves around customers and markets, we conduct dialogues with our stakeholders in order to explore common ground for addressing societal challenges, building partnerships and jointly developing supporting ecosystems for our innovations around the world. An overview of stakeholders and topics discussed is provided in [chapter 13, Sustainability statements](#), of this Annual Report.

For more information on our stakeholder engagement activities in 2017, please refer to [sub-section 13.3.8, Stakeholder engagement](#), of this Annual Report.

3.2.11 Supplier sustainability

Royal Philips has a direct business relationship with approximately 4,600 product and component suppliers and 18,000 service providers. In many cases the sustainability issues deeper in our supply chain require us to intervene beyond tier 1 of the chain.

Supplier sustainability strategy

Managing our large and complex supply chain in a socially and environmentally responsible way requires a structured and innovative approach while being transparent and engaging with a wide variety of stakeholders. Insights gained through our regular stakeholder engagement process are used as an input to manage our supplier sustainability strategy.

Please refer to [sub-section 13.3.9, Supplier indicators](#), of this Annual Report and to the Philips supplier sustainability [website](#) for more details on the Philips supplier sustainability program.

3.3 Environmental performance

Philips has a long sustainability history stretching all the way back to our founding fathers. In 1994, we launched our first program and set sustainability targets for our own operations. Next, we launched our second program in 1998, which focused on the environmental dimension of our operations and products. We also started to focus on sustainability in our supply chain in 2003. We extended our scope further in 2010 by including the social dimension of products and solutions, which is now reflected in our company vision:

We strive to make the world healthier and more sustainable through innovation. Our goal is to improve the lives of 3 billion people a year by 2025.

In 2016, our CEO Frans van Houten launched our new five-year sustainability program, 'Healthy people, sustainable planet', addressing both social and environmental challenges and including associated targets to be achieved by 2020.

The three pillars of the 'Healthy people, sustainable planet' program are:

- Creating value for our customers through **Sustainable Solutions**
- Leading by example in our **Sustainable Operations**
- Multiplying our impact by driving **Sustainability through our supply chain**

More details on the program, as well as the results in 2017, have been addressed in this report.

Every year, Royal Philips publishes a full Integrated Annual Report. Our independent auditor Ernst & Young (EY) has not only audited our financial information but has also provided reasonable (highest level) assurance on Sustainability Information in [chapter 13, Sustainability statements](#), of this Annual Report and sections [section 3.2, Social performance](#), of this Annual Report and [section 3.3, Environmental performance](#), of this Annual Report. Please refer to [section 13.5, Assurance report of the independent auditor](#), of this Annual Report. With this, Philips is a frontrunner in this field.

In this Environmental performance section an overview is given of the most important environmental parameters of the new program. Improving people's lives, Health and Safety, and Supplier Sustainability are addressed in the Social performance section. Details of the 'Healthy people, sustainable planet' parameters can be found in the [chapter 13, Sustainability statements](#), of this Annual Report.

Environmental impact

Philips has been performing Life-Cycle Assessment (LCAs) since the 1990s. These assessments provide insight into the environmental impacts of our products from cradle to grave, including the supply chain, manufacturing process at Philips, use phase and disposal phase. The insights are used to steer our EcoDesign efforts and to grow our Green solutions portfolio.

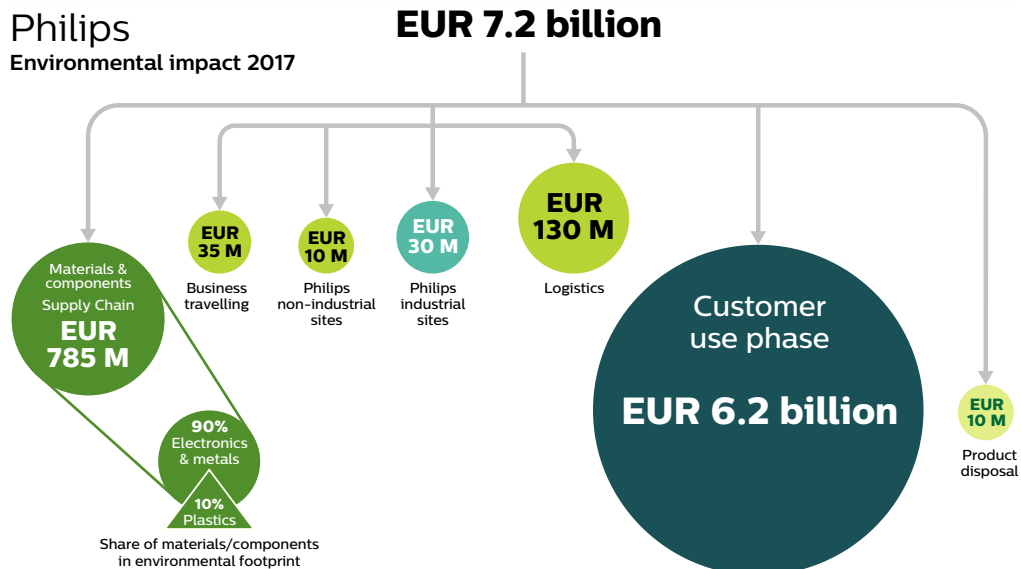
As a logical next step we have measured our environmental impact on society at large via a so-called Environmental Profit & Loss (EP&L) account which includes the hidden environmental costs associated with our activities and products, again from cradle to grave. It will support our 'Healthy people, sustainable planet' program by providing insights into the main environmental hotspots from an overall business point of view.

The EP&L account is based on LCA methodology in which the environmental impacts are expressed in monetary terms using conversion factors as developed by [CE Delft](#). We used expert opinions and estimates for some parts of the calculations. The figures reported are Philips' best possible estimate. As we gain new insights and retrieve more and better data, we may enhance the methodology and accuracy of results in the future. For more information we refer to our [methodology report](#).

The current EP&L account only includes the hidden environmental costs along the complete lifecycle of our products and solutions. It does not yet include the benefits to society that Philips generates by improving people's lives through our products and solutions, e.g. our healthcare or healthy food preparation solutions. We have a well-established methodology to calculate the number of lives we positively touch with our products and solution. It is our aim to look into valuing these societal benefits in monetary terms as well and include them in our future EP&L account, where possible.

Results 2017

In 2017, Philips had an environmental impact (loss) of EUR 7.2 billion of which EUR 200 million (3%) is directly caused by Philips' own operations, mainly driven by energy consumption at our factories. The main environmental impact, 86% of total, is related to the usage of our products which is due to electricity consumption. Particulate matter formation and climate change are the main environmental impacts accounting for respectively 43% and 28% of the total impact.



Conceptual drawing, areas do not reflect actual proportions

The environmental loss includes the environmental impact of the full life-time of our products that we put on the market in 2017, e.g. an average 7 years of usage in case of a vacuum cleaner or 10 years on average in case of a MRI system.

The environmental loss has been positively influenced over the years by our efforts to increase the energy efficiency of our products. This will be enhanced by society's transition to a renewable energy system. We also expect a shift in our environmental impact from the use phase to our supply chain, i.e. the materials we use in our products. Our supply chain currently has an environmental impact of some EUR 800 million, which is 11% of our total environmental impact. The main contributors are the electronic components, cables and steel used in our products. Through our Circular Economy and Supplier Sustainability programs we will continue to focus on reducing the environmental impact caused by the materials we source and apply in our products.

3.3.1 Green Innovation

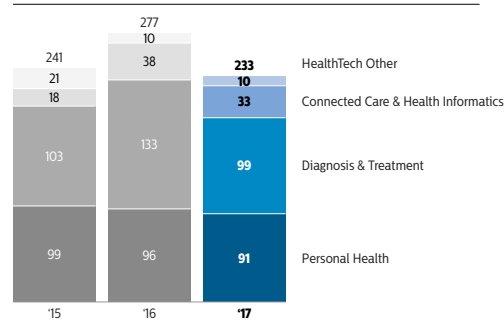
Green Innovation is the Research & Development spend related to the development of new generations of Green Products and Solutions and Green Technologies.

Sustainable Innovation is the Research & Development spend related to the development of new generations of products and solutions that address the United Nations' Sustainable Development Goals 3 ("to ensure healthy lives and promote well-being for all at all ages") or 12 ("to ensure sustainable consumption and production patterns"). With regard to the latter, Philips

set a target of EUR 7.5 billion (cumulative) for its health technology businesses for the period 2016 - 2020 as part of the 'Healthy people, sustainable planet' program.

In 2017, Philips invested EUR 233 million in Green Innovation while the health technology businesses invested some EUR 1.4 billion in Sustainable Innovation.

Philips Group
Green Innovation per segment in millions of EUR
2015 - 2017



Diagnosis & Treatment businesses

Philips develops innovative diagnosis and treatment solutions that enable first-time right diagnosis, precision interventions and therapy, while respecting the boundaries of natural resources. Investments in Green Innovation in 2017 amounted to EUR 99 million, a decrease compared to 2016, as a number of large innovation projects had been completed in 2016. All Philips Green Focal Areas are taken into account as we

aim to reduce environmental impact over the total lifecycle. Energy efficiency is an area of focus, especially for our large imaging systems such as MRI. Philips also pays particular attention to enabling the upgrading of pathways, so our customers can benefit from the most advanced enhancements in workflow, dose management, and imaging quality with the equipment that they already own which enables reduced materials use and lower cost. Our Diagnosis & Treatment businesses actively support a voluntary industry initiative to improve the energy efficiency of medical imaging equipment. Moreover, we are actively partnering with multiple leading care providers to look together for innovative ways to reduce the environmental impact of healthcare, for example by maximizing energy-efficient use of medical equipment and optimizing lifecycle value.

Connected Care & Health Informatics businesses

Philips innovates with connected health IT solutions that integrate, collect, combine and deliver quality data for actionable insights to help improve access to quality care, while respecting the boundaries of natural resources. It is our belief that well-designed e-health solutions can reduce the travel-related carbon footprint of healthcare, and improve access to care and outcomes. Investments in Green Innovation in 2017 amounted to EUR 33 million, in line with previous years. All Philips Green Focal Areas are taken into account as we aim to reduce environmental impact over the total lifecycle. Energy efficiency and material reduction are the main areas of focus.

Personal Health businesses

Continuous high R&D investments at our Personal Health businesses are also reflected in Green Innovation spend, which amounted to EUR 91 million in 2017, compared with EUR 96 million in 2016. The investments resulted in high Green Revenues in all business groups. The Personal Health businesses continued their work on improving the energy efficiency of their products, closing the materials loop (e.g. by using recycled materials in products and packaging) and the voluntary phase-out of polyvinyl chloride (PVC), brominated flame retardants (BFR), Bisphenol A (BPA) and phthalates from, among others, food contact products. A breakthrough has been achieved with the implementation of PVC-free internal wiring in our SENSEO® portfolio and the application of recycled plastics in our air purification and coffee portfolio. Regarding the phase-out of PVC/BFR, close to 100% of the oral healthcare, mother and child care, male grooming, skincare and female depilation products are PVC/BFR-free. Our new green battery-charged devices outperform the most stringent energy efficiency standard in the world (USA Federal).

HealthTech Other

HealthTech Other invested EUR 10 million in Green Innovations, spread over projects focused on global challenges related to water, air, energy, food, Circular Economy, and access to affordable healthcare. The Research organization within HealthTech Other used the Sustainable Innovation Assessment tool, in which innovation projects are evaluated and scored along environmental and social dimensions, in order to identify those projects that most strongly drive sustainability. Transfers of Research projects include a Lives Improved calculation to assess what the project's contribution will be to Philips' vision to improve the lives of 3 billion people a year by 2025. In a Philips Research demonstration project, for example, a new and innovative 'Philips Unified Monitoring Architecture' was developed containing standardized components for next-generation patient monitoring, which helps streamline workflows and improve monitoring across the health continuum. Sustainability impact assessment has shown significant improvements in both environmental and social areas. This could be realized by smart concepts for smaller low-power and light-weight modules, and increased battery lifetimes. Herewith a sustainability improvement of over 30% has been demonstrated, while avoiding restricted materials.

Circular Economy

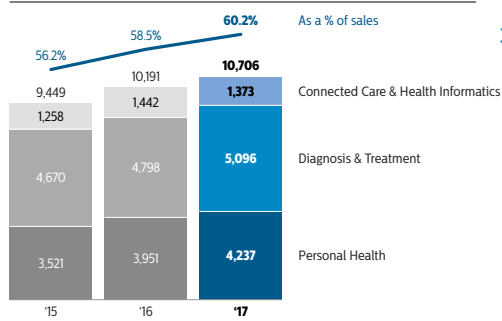
The transition from a linear to a circular economy is essential if we are to create a sustainable world. A circular economy aims to decouple economic growth from the use of natural resources and ecosystems by using these resources more effectively. It is a driver of innovation in the areas of material, component and product re-use, as well as new business models such as system solutions and services. In a circular economy, more effective (re)use of materials enables the creation of more value, both by means of cost savings and by developing new markets or growing existing ones. The 'Healthy people, sustainable planet' program includes a target to generate 15% of our revenues in 2020 from circular products and solutions.

For more information on our Circular Economy activities and the progress towards targets in 2017, please refer to [sub-section 13.4.1, Circular Economy](#), of this Annual Report.

3.3.2 Green Revenues

Green Revenues are generated through products and solutions which offer a significant environmental improvement in one or more Green Focal Areas: Energy efficiency, Packaging, Hazardous substances, Weight, Circularity, and Lifetime reliability. Green Revenues increased to EUR 10.7 billion in 2017, or 60.2% of sales (58.5% in 2016), thereby reaching a record level for Philips.

Philips Group
Green Revenues per segment
 in millions of EUR unless otherwise stated
 2015 – 2017



Through our EcoDesign process we aim to create products and solutions that have significantly less impact on the environment during their whole lifecycle. Overall, the most significant improvements have been realized in our energy efficiency Green Focal Area, an important objective of our program, although there was also growing attention for hazardous substances and recyclability in all segments in 2017, the latter driven by our Circular Economy initiatives.

Diagnosis & Treatment businesses

In 2017, our Diagnosis & Treatment businesses maintained their Green Product and Solutions portfolio with redesigns of various Green Products with further environmental improvements. These products improve patient outcomes, provide better value, and help secure access to high-quality care, while reducing environmental impact. We received third-party confirmation in 2017 that the Philips portfolio of 1.5T MRI scanners leads the industry in terms of their energy efficiency according to the COCIR SRI methodology.

Connected Care & Health Informatics businesses

Our Connected Care & Health Informatics businesses maintained its Green Product and Solutions portfolio in 2017.

Personal Health businesses

Our Personal Health businesses focus on Green Products and Solutions which meet or exceed our minimum requirements in the areas of energy consumption, packaging, and substances of concern. Green Revenues in 2017 surpassed 58% of total sales, compared to 56% in 2016. All our new consumer Green Products with rechargeable batteries (like toothbrushes, shavers, and grooming products) outperform the world's most stringent energy efficiency norm set by the US Federal government. We are making steady progress in developing PVC/BFR-free products. More than 70% of our consumer product sales consist of PVC/BFR-free products, with the exception of the power cords, for which there are not yet economically viable alternatives available. In the remaining 30% of

consumer product sales, PVC/BFR has already been phased out to a significant extent, but the products are not yet completely free of these substances.

3.3.3 Sustainable Operations

Philips' Sustainable Operations programs focus on the main contributors to climate change, recycling of waste, reduction of water consumption, and reduction of emissions. Full details can be found in [chapter 13, Sustainability statements](#), of this Annual Report.

Carbon footprint and energy efficiency

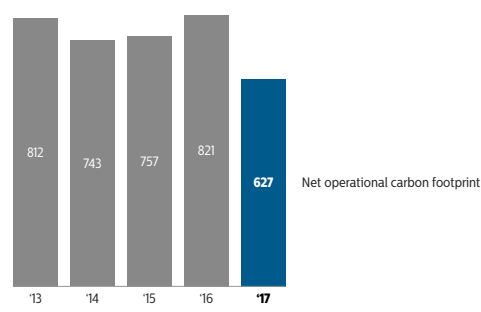
Philips has committed to the ambition of becoming 100% carbon-neutral in our operations and sourcing all our electricity usage from 100% renewable sources by 2020.

As of 2008, Philips reports its climate performance to CDP (formerly known as the Carbon Disclosure Project), a global NGO that assesses the greenhouse gas (GHG) emission performance and management of reporting companies. For the fifth year in a row we received the Climate Leadership (A) score in 2017. In order to deliver on the carbon neutrality commitment we have set ambitious reduction targets.

In 2017, our greenhouse gas emissions resulted in 847 kilotonnes of carbon dioxide-equivalent (CO₂e), but because of our carbon neutrality program, some of our emissions have been compensated for via carbon offsets, resulting in a total of 627 kilotonnes carbon dioxide-equivalent (CO₂e).

Philips reports all its emissions in line with the Greenhouse Gas Protocol (GHGP) as further described in [chapter 13, Sustainability statements](#), of this Annual Report.

Philips Group
Net operational carbon footprint
 in kilotonnes CO₂-equivalent
 2013 – 2017



In 2017, our operational carbon intensity (in tonnes CO₂e/EUR million sales) improved by 2%, even as our company recorded 4% comparable sales growth. This still excludes the acquired carbon offsets. As part of our

'Healthy people, sustainable planet' program we are continuing our efforts to decouple economic growth from our environmental impact.

The significant reductions in our scope 2 (indirect) emissions are mainly driven by our increased global renewable electricity share from 62% in 2016 to 79% in 2017.

We achieved a major milestone as 100% of our US operations are now powered by renewable electricity from the Los Mirasoles windfarm. In addition, our renewable electricity purchasing consortium with AkzoNobel, DSM and Google closed the second wind energy transaction in the Netherlands in 2017 – the Bouwdokken windfarm in the province of Zeeland. We expect the first Dutch wind energy to be delivered in 2018 and the two Dutch windfarms will power all our operations in the Netherlands by 2019.

Combined with the achieved energy reductions this led to a 53% carbon reduction from our electricity consumption (scope 2) in 2017 compared to 2016.

Our business travel emissions showed a reduction of 15% compared to 2016, driven by an air travel limitation introduced in 2017, which led to an air travel emission reduction of 9%. The emissions resulting from our lease cars decreased by 23% and the emissions from rental cars went down by 5%. In order to further decrease our business travel emissions we will continue to promote video conferencing as an alternative to travel, promote alternative modes of transport and set new fuel efficiency targets in our lease car policy.

As our sales grew, we recorded an increase of 23% in our logistics operations compared to 2016. This mainly resulted from a strong increase in air freight shipments to meet demand. We plan to introduce various measures to drive down air freight shipments by introducing a stricter air freight policy and by optimizing our warehouse locations.

In 2017 we kicked off our carbon neutrality program by compensating 220 kilotonnes of carbon emissions, equivalent to the annual uptake of approximately 6 million medium-sized oak trees. This covers the total emissions of our direct emissions in our sites, all our business travel emissions and part of our logistics emissions. We do so by financing carbon reduction projects in emerging regions that have a strong link with SDG 3 and SDG 12.

We are investing in several carbon emission reduction projects to gradually drive down our emissions to zero by 2020. We have selected projects in emerging regions that, in addition to generating emission reductions, also drive social, economic and additional environmental progress for the communities in which they operate, such as:

Providing access to safe drinking water while reducing wood consumption

These carbon emission reduction projects will provide millions of liters of safe drinking water in Uganda and Ethiopia and will reduce the mortality risk from water-borne diseases. Additionally, less wood will be required for boiling water, leading to less indoor air pollution and slowing down the deforestation rate.

Fighting against respiratory diseases and deforestation by clean cookstoves

By financing high-efficient cookstoves in Kenya and Uganda, less wood will be required for cooking, leading to lower carbon emissions, a reduction in diseases caused by indoor air pollution and a lower deforestation rate in these regions.

Providing access to clean energy while improving health and education

This project will reduce the demand-supply gap in the Dewas region in India and will provide renewable energy to more than 50,000 households. The project will also provide a mobile medical unit in 24 villages, giving diagnosis and medicines free of charge twice a month. Additional funding will be provided to educational programs and improving sanitation facilities in five local schools to maximize the social impact.

Philips Group
Operational carbon footprint by scope
in kilotonnes CO₂-equivalent
2013 – 2017

	2013	2014	2015	2016	2017
Scope 1	44	40	39	42	38
Scope 2 (market based)	114	109	106	121	58
Scope 2 (location based)	213	210	212	252	225
Scope 3	654	594	612	658	751
Total (scope 1, 2 (market based), and 3)	812	743	757	821	847
Emissions compensated by carbon offset projects	0	0	0	0	220
Net operational carbon emissions	812	743	757	821	627

During 2017, the applied emission factors used to calculate our operational carbon footprint have been updated with the latest DEFRA (UK Department for Environment, Food & Rural Affairs) 2017 emission factors. Philips reports all its emissions in line with the Greenhouse Gas Protocol (GHGP) as further described in Sustainability statements.

Philips Group
Ratios relating to carbon emissions and energy use
2013 – 2017

	2013	2014	2015	2016	2017
Operational CO₂ emissions in kilotonnes CO ₂ -equivalent	812	743	757	821	847
Operational CO₂ efficiency in tonnes CO ₂ - equivalent per million EUR sales	57.27	53.36	46.58	48.48	47.64
Operational energy use in terajoules	5,918	5,747	5,639	5,526	4,858
Operational energy efficiency in terajoules per million EUR sales	0.42	0.41	0.35	0.33	0.27

Water

Total water intake in 2017 was 888,000 m³, about 8% lower than in 2016. Personal Health, which consumes 56% of total water usage recorded a 19% decrease. This decrease was mainly due to a relocation of one of the manufacturing sites in China and water-saving actions in various locations. The decrease was partially mitigated by increases in other sites due to production volume increases.

Philips Group
Water intake in thousands of m³
2013 – 2017

	2013	2014	2015	2016	2017
Personal Health	652	585	614	613	496
Diagnosis & Treatment	311	392	268	269	312
Connected Care & Health Informatics	77	74	94	81	80
Philips Group	1,040	1,051	976	963	888

In 2017, 97% of water was purchased and 3% was extracted from groundwater wells.

Waste

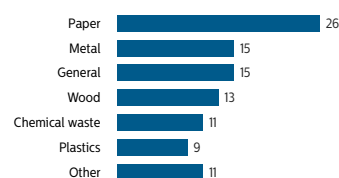
In 2017, total waste decreased by 1% compared to 2016 to 24.6 kilotonnes, mainly due to operational changes and less packaging waste. The Personal Health businesses contributed 61% of total waste, Diagnosis & Treatment businesses 34% and Connected Care & Health Informatics businesses 5%. The reported increase in waste in the Personal Health businesses was mainly caused by higher production volumes.

Philips Group
Total waste in kilotonnes
2013 – 2017

	2013	2014	2015	2016	2017
Personal Health	13.2	13.1	13.8	14.3	15.1
Diagnosis & Treatment	6.7	6.8	8.0	9.2	8.3
Connected Care & Health Informatics	1.1	1.2	1.4	1.4	1.2
Philips Group	21.0	21.1	23.2	24.9	24.6

Total waste consists of waste that is delivered for landfill, incineration or recycling. Our sites are addressing both the recycling percentage as well as waste sent to landfill as part of the new sustainability program. Materials delivered for recycling via an external contractor amounted to 20 kilotonnes, which equals 80% of total waste, comparable to 2016. Of the 20% remaining waste, 83% comprised non-hazardous waste and 17% hazardous waste. Our Zero Waste to Landfill KPI excludes one-time-only waste and waste delivered to landfill due to regulatory requirements. According to this definition, in 2017 we reported 2.5 kilotonnes of waste sent to landfill. 17 out of our 38 industrial sites achieved Zero Waste to Landfill status.

Philips Group
Industrial waste delivered for recycling in %
2017



Emissions

In the 'Healthy people, sustainable planet' program, Royal Philips included new reduction targets for the substances that are most relevant for its businesses. In order to provide comparable information at Group level, please find the summary of the emissions of the formerly targeted substances below. Emissions of restricted substances were reduced from 1 kilos in 2016 to zero in 2017, mainly caused by one site in China which phased out a thinner containing benzene. The level of emissions of hazardous substances decreased from 10,496 kilos in 2016 to 5,243 kilos in 2017 (-50%), mainly driven by changes in the lacquering process and product mix in the Personal Health businesses.

Philips Group
Restricted and hazardous substances in kilos
2013 – 2017

	2013	2014	2015	2016	2017
Restricted substances	29	20	18	1	-
Hazardous substances	27,262	24,712	22,394	10,496	5,243

For more details on emissions from substances, please refer to [sub-section 13.4.3, Sustainable Operations](#), of this Annual Report.

3.4 Our commitment to Quality

We continue to drive quality and regulatory performance improvement throughout the Philips Group. Under our governance model, the Executive Committee is ultimately accountable for Quality at Philips, supported by the Quality & Regulatory team. The Quality & Regulatory team drives to one common

set of standards through the Philips Quality Management System (PQMS), as well as providing transparency on performance and opportunities for further improvement. Inclusion of quality metrics in monthly business reviews has driven transparency and improvement execution.

Our year-over-year performance continues to show improvement. On key end-to-end transformation initiatives, we progressed significantly in 2017, including making headway with the implementation of PQMS for all business groups.

However, 2017 was also an eventful year from a regulatory compliance perspective:

- In August 2017, the Food and Drug Administration (FDA) conducted an inspection of Philips' Computed Tomography/Advanced Molecular Imaging (CT/AMI) facility in Cleveland, Illinois. This was the first FDA inspection of the site since the temporary, voluntary suspension of manufacturing and shipping of CT/AMI products from Cleveland in 2014. Following the inspection, Philips submitted its response to the inspectional observations for review by the FDA. In December 2017, the company had a constructive meeting with the FDA. Philips will provide monthly status reports to the FDA on its progress in addressing the observations.
- In October 2017, Philips entered into a consent decree with the US Department of Justice, representing the FDA, related to compliance with current good manufacturing practice requirements arising from past inspections in and before 2015, focusing primarily on Philips' Emergency Care & Resuscitation (ECR) business operations in Andover (Massachusetts, US) and Bothell (Washington, US). The decree also provides for increased scrutiny, for a period of time, of the compliance of the other patient care businesses at these facilities with the Quality System Regulation. Under the decree, Philips has suspended the manufacturing and distribution of external defibrillators manufactured at these facilities, subject to certain exceptions, until FDA certifies through inspection the facilities' compliance with the Quality System Regulation. The decree allows Philips to continue the manufacture and distribution of certain automated external defibrillator (AED) models and Philips will continue to service ECR devices and provide consumables and the relevant accessories.

We are fully engaged with FDA staff concerning both matters and anticipate follow-up inspections of these facilities by FDA in 2018 after further compliance improvements have been made.

Currently we are also focusing on the European Union Medical Devices Regulation (EU MDR) compliance for future market access, and early identification and collaboration in the changing regulatory environment.

Looking ahead we will continue to raise the performance bar, also including Quality in the evaluation of all senior management. With consistency of purpose, top-down accountability, standardization, and leveraging continuous improvement we aim to drive greater speed in the adoption of a Quality mindset throughout the enterprise.

3.5 Proposed distribution to shareholders

Pursuant to article 34 of the articles of association of Royal Philips, a dividend will first be declared on preference shares out of net income. The remainder of the net income, after any retention by way of reserve with the approval of the Supervisory Board, shall be available for distribution to holders of common shares subject to shareholder approval after year-end. As of December 31, 2017, the issued share capital consists only of common shares; no preference shares have been issued. Article 33 of the articles of association of Royal Philips gives the Board of Management the power to determine what portion of the net income shall be retained by way of reserve, subject to the approval of the Supervisory Board.

A proposal will be submitted to the upcoming Annual General Meeting of Shareholders to declare a dividend of EUR 0.80 per common share (up to EUR 750 million if all shareholders would elect cash), in cash or in shares at the option of the shareholder, against the net income for 2017.

If the above dividend proposal is adopted, the shares will be traded ex-dividend as of May 7, 2018 at the New York Stock Exchange and Euronext Amsterdam. In compliance with the listing requirements of the New York Stock Exchange and the stock market of Euronext Amsterdam, the dividend record date will be May 8, 2018.

Shareholders will be given the opportunity to make their choice between cash and shares between May 9, 2018 and June 1, 2018. If no choice is made during this election period the dividend will be paid in cash. On June 1, 2018 after close of trading, the number of share dividend rights entitled to one new common share will be determined based on the volume weighted average price of all traded common shares Koninklijke Philips N.V. at Euronext Amsterdam on May 30 and 31, and June 1, 2018. The Company will calculate the number of share dividend rights entitled to one new common share (the 'ratio'), such that the gross dividend in shares will be approximately equal to the gross dividend in cash. The ratio and the number of shares to be issued will be announced on June 5, 2018. Payment of the dividend and delivery of new common shares, with settlement of fractions in cash, if required, will take place from June 6, 2018. The distribution of dividend in cash to holders of New York Registry shares will be made in USD at the USD/EUR rate as per WM/ Reuters FX Benchmark 2 PM CET fixing of June 4, 2018.

Further details will be given in the agenda for the 2018 Annual General Meeting of Shareholders. All dates mentioned remain provisional until then.

Dividend in cash is in principle subject to 15% Dutch dividend withholding tax, which will be deducted from the dividend in cash paid to the shareholders. Dividend in shares paid out of net income and retained earnings is subject to 15% dividend withholding tax, but only in respect of the par value of the shares (EUR 0.20 per share).

In 2017, a dividend of EUR 0.80 per common share was paid in cash or shares, at the option of the shareholder. For 48.3% of the shares, the shareholders elected for a share dividend resulting in the issue of 11,264,163 new common shares, leading to a 1.2% dilution. EUR 384 million was paid in cash. See also [chapter 15, Investor Relations](#), of this Annual Report.

The balance sheet presented in this report, as part of the Company financial statements for the period ended December 31, 2017, is before appropriation of the result for the financial year 2017.

4 Segment performance

Our structure in 2017

Koninklijke Philips N.V. ('Royal Philips' or the 'Company') is the parent company of the Philips Group ('Philips' or the 'Group'), headquartered in Amsterdam, the Netherlands. The Company is managed by the members of the Executive Committee (comprising the Board of Management and certain key officers) under the supervision of the Supervisory Board. The Executive Committee operates under the chairmanship of the Chief Executive Officer and shares responsibility for the deployment of Philips' strategy and policies, and the achievement of its objectives and results.

In September 2014, Philips announced its plan to sharpen its strategic focus by establishing two stand-alone companies focused on the HealthTech and Lighting opportunities respectively. To this end, a stand-alone structure was established for Philips Lighting within the Philips Group, effective February 1, 2016. Then, on May 27, 2016, Philips Lighting was listed

and started trading on Euronext in Amsterdam under the symbol 'LIGHT'. Following the listing of Philips Lighting, Philips retained a 71.225% stake. In the course of 2017, Philips gradually reduced its stake in Philips Lighting's issued share capital to approximately 29.01%, in line with its stated objective to fully sell down its stake in Philips Lighting within one year.

Following the latter accelerated bookbuild offering on November 28, 2017, Philips no longer has control over Philips Lighting and ceased to consolidate Philips Lighting as from the end of November 2017.

The reportable segments are Personal Health businesses, Diagnosis & Treatment businesses, and Connected Care & Health Informatics businesses, each being responsible for the management of its business worldwide. Additionally, Philips identifies HealthTech Other and Legacy Items, as shown below:

Personal Health businesses	Diagnosis & Treatment businesses	Connected Care & Health Informatics businesses	HealthTech Other	Legacy Items
Health & Wellness Personal Care Domestic Appliances Sleep & Respiratory Care	Diagnostic Imaging Image-Guided Therapy Ultrasound	Patient Care & Monitoring Solutions Healthcare Informatics Population Health Management	Innovation Emerging Businesses IP Royalties Central costs Other	Legacy litigation Separation cost
Focus of external reporting				

4.1 Personal Health businesses

Egbert van Acht was appointed Chief Business Leader of the Personal Health businesses effective October 1, 2017, succeeding Pieter Nota. Egbert joined Philips in 2002 and has held various senior leadership roles in the company. Most recently, he led the Health & Wellness business group for seven years. Egbert started his career at Procter & Gamble.

4.1.1 About Personal Health businesses

Our Personal Health businesses play an important role on the health continuum – in the healthy living, prevention and home care stages – delivering integrated, connected solutions that support healthier lifestyles and those living with chronic disease.

Leveraging our deep consumer expertise and extensive healthcare know-how, we enable people to live a healthy life in a healthy home environment, and to proactively manage their own health.

Through our various businesses, Personal Health has delivered sustained strong growth and margin expansion in recent years, driven by five main factors:

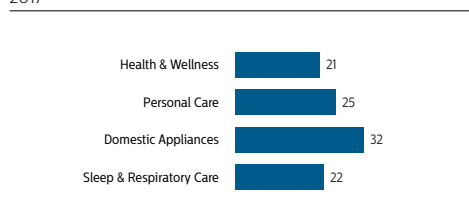
- Share gains in growing markets
- Geographical expansion with proven propositions
- Innovation at the forefront of digital health
- High-impact consumer marketing programs
- Leadership in online sales

Through 2017, we have driven above-market growth and stepped up profitability into the mid-teens, building on a strong track record. Personal Health has many distinct product categories and associated competitors, including Procter & Gamble in Personal Care and Oral Healthcare, Groupe SEB in Domestic Appliances and ResMed in Sleep & Respiratory Care.

In 2017, the Personal Health segment consisted of the following areas of business:

- **Health & Wellness:** mother and child care, oral healthcare
- **Personal Care:** male grooming, beauty
- **Domestic Appliances:** kitchen appliances, coffee, air, garment care, floor care
- **Sleep & Respiratory Care:** sleep, respiratory care, respiratory drug delivery

Personal Health
Total sales by business as a %
2017



Through our Personal Health businesses, we offer a broad range of products in various consumer price segments, always aiming to realize premium value. We continue to expand our portfolio and increase its accessibility, particularly in lower-tier cities in growth geographies. We are well positioned to capture further growth in online sales and continue to build our digital and e-commerce capabilities. We also continue to roll-out high-impact consumer marketing programs in support of key innovations. In 2017, we further rolled out Philips OneBlade, accompanied by an innovative Digital Advocacy Marketing Program, for which we received a Euro Gold Effie Award 2017 in the category 'Product/Service launch'.

The company's wide portfolio of connected consumer health platforms – such as uGrow, DiamondClean Smart and DreamFamily – leverages Philips HealthSuite, a cloud-enabled connected health ecosystem of devices, apps and digital tools that enable personalized health and continuous care.

We are leveraging connectivity to engage consumers in new and impactful ways through social media and digital innovation. For example, in 2017 we launched the Philips Sonicare DiamondClean Smart toothbrush, a complete oral care solution for a healthier mouth. This toothbrush gives users exceptional results thanks to new, high-performance brush heads and personalized coaching enabled by smart sensor technology. Via the Philips HealthSuite digital platform, the app is a virtual hub for personal oral healthcare, enabling users to manage their brushing and breath quality on a daily basis, share results with their dental practitioners, and receive personalized guidance and advice.

Under normal economic conditions, Philips' Personal Health businesses experience seasonality, with higher sales in the fourth quarter.

In 2017, Personal Health employed 23,170 people worldwide. The global sales and service organization covered more than 50 mature and growth geographies. In addition, we operated manufacturing and business creation organizations in Argentina, Austria, Brazil, China, India, Indonesia, Italy, the Netherlands, Romania, the UK and the US.

Philips' Personal Health businesses are subject to regulatory requirements in the markets where they operate. This includes the European Union's Waste from Electrical and Electronic Equipment (WEEE), Restriction of Hazardous Substances (RoHS), Registration, Evaluation, Authorization and Restriction of Chemicals (REACH), Energy-using Products (EuP) requirements and Product Safety Regulations. We have a growing portfolio of medically regulated products in our Health & Wellness, Personal Care and Sleep & Respiratory Care businesses. For these products we are subject to the applicable requirements of the US FDA, the European Medical Device Directive, the CFDA in

China and comparable regulations in other countries. Through our growing beauty, oral healthcare and mother and child care product portfolio the range of applicable regulations has been extended to include requirements relating to cosmetics and, on a very small scale, pharmaceuticals.

With regard to quality, please refer to [section 3.4, Our commitment to Quality](#), of this Annual Report.

With regard to sourcing, please refer to [sub-section 13.3.9, Supplier indicators](#), of this Annual Report.

4.1.2 2017 business highlights

At the International Dental Show in Germany, the world's leading trade fair for the dental sector, Philips introduced the Philips Sonicare DiamondClean Smart toothbrush and Philips Sonicare Breath care system with breath analyzer, an all-in-one connected oral care platform. Philips also presented the results of a new clinical study demonstrating the effectiveness of Philips Sonicare power toothbrushes and Philips AirFloss Ultra.

Philips acquired UK-based Health & Parenting, a leading developer of mobile applications for expectant and new parents, used by one in two expectant mothers in the UK.

As a driver of new care models, Philips teamed up with leading telehealth provider American Well to jointly deliver virtual care solutions around the world by embedding American Well's mobile telehealth services into an array of Philips solutions, starting with the Philips Avent uGrow parenting platform, giving parents 24/7 access to professional medical consultations.

Launched less than two years ago, the revolutionary OneBlade hybrid styler, which can trim, edge and shave any length of male facial hair, generated annual sales of more than EUR 100 million within 18 months of its launch.

Building on the company's market-leading propositions in healthy eating, Philips launched the latest generation of the Philips Airfryer, which features an innovative technology to prepare tasty, healthier food with little to no oil. As a leader in this category, Philips has sold close to 10 million Airfryers globally to date.

Philips' Sleep & Respiratory Care business continues to grow in respiratory care, with strong acceptance of its market-leading home ventilation offerings. This portfolio was further extended with the launch of the connected Trilogy ventilator in North America, linking it to Philips' unique patient management solution Care Orchestrator. In sleep care, continued mask share gains were driven by strong traction of the DreamWear family of masks, including the recently introduced DreamWear Pillow mask.

Philips acquired Respiratory Technologies, a US-based provider of an innovative airway clearance solution for patients with chronic respiratory conditions.

In China, Philips partnered with Oranger, a service provider specialized in chronic respiratory disease management, and Health 100, the largest health examination organization in China, to provide integrated solutions for chronic respiratory diseases that cover screening, referral, treatment and recovery. As part of the agreement, Philips acquired a minority interest in Oranger.

Building on its strategy to deliver relevant solutions and business models, Philips acquired Australian Pharmacy Sleep Services (APSS), a pioneer in pharmacy sleep testing. APSS will complement Philips' sleep and respiratory care portfolio and will help to accelerate the business's home sleep testing offering through the pharmacy channel in Australia.

4.1.3 Financial performance

Net income is not allocated to segments as certain income and expense line items are monitored on a centralized basis.

Personal Health
Key data in millions of EUR unless otherwise stated
2015 – 2017

	2015	2016	2017
Sales	6,751	7,099	7,310
Sales growth			
Nominal sales growth	14%	5%	3%
Comparable sales growth ¹⁾	5%	7%	6%
Income from operations	736	953	1,075
as a % of sales	10.9%	13.4%	14.7%
Adjusted EBITA ¹⁾	966	1,108	1,221
as a % of sales	14.3%	15.6%	16.7%

¹⁾ Non-IFRS financial measure. For the definition and reconciliation to the most directly comparable IFRS measure, refer to [chapter 5, Reconciliation of non-IFRS information](#), of this Annual Report

In 2017, sales amounted to EUR 7,310 million, a nominal increase of 3% compared to 2016. Excluding a 3% negative currency impact, comparable sales¹⁾ were 6% higher year-on-year, driven by high-single-digit growth in Health & Wellness and mid-single-digit growth in Sleep & Respiratory Care, Domestic Appliances and Personal Care. Green Revenues amounted to EUR 4,237 million, or 58% of total segment sales.

Sales in growth geographies increased 7% on a nominal basis and on a comparable basis¹⁾ growth geographies showed double-digit growth, reflecting double-digit growth in Latin America, Middle East & Turkey and India, and high-single-digit growth in China and Central & Eastern Europe. Mature geographies increased 1% on a nominal basis and on a comparable basis recorded low-single-digit growth, driven by mid-single-digit

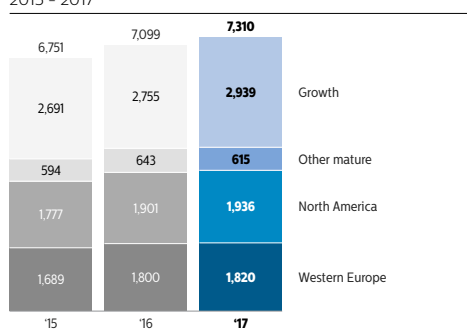
¹⁾ Non-IFRS financial measure. For the definition and reconciliation to the most directly comparable IFRS measure, refer to [chapter 5, Reconciliation of non-IFRS information](#), of this Annual Report.

growth in Western Europe and low-single-digit growth in North America, partly offset by a low-single-digit decline in other mature geographies.

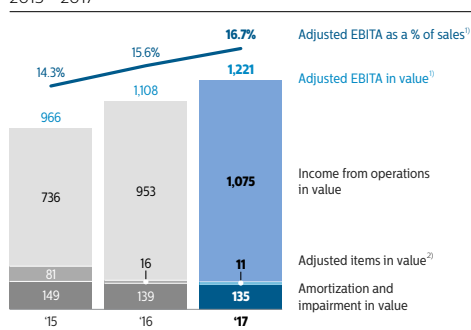
Income from operations in 2017 increased to EUR 1,075 million, or 14.7% of sales compared to EUR 953 million, or 13.4% of sales in 2016. The year 2017 included EUR 136 million of amortization charges, mainly related to intangible assets in Sleep & Respiratory Care, compared to 2016 which include EUR 139 million of amortization charges, mainly related to intangible assets at Sleep & Respiratory Care. Restructuring and acquisition-related charges were EUR 11 million, compared to EUR 16 million in 2016.

Adjusted EBITA¹⁾ increased by EUR 113 million or 110 basis points as a % of sales compared to 2016. The increase was attributable to higher volumes and procurement savings, partly offset by investments in advertising and promotion.

Personal Health
Sales per geographic cluster in millions of EUR
2015 – 2017



Personal Health
Income from operations and Adjusted EBITA¹⁾
in millions of EUR unless otherwise stated
2015 – 2017



¹⁾ Non-IFRS financial measure. For the definition and reconciliation to the most directly comparable IFRS measure, refer to chapter 5, Reconciliation of non-IFRS information, of this Annual Report

²⁾ Adjusted items include restructuring, acquisition-related and other charges

¹⁾ Non-IFRS financial measure. For the definition and reconciliation to the most directly comparable IFRS measure, refer to chapter 5, Reconciliation of non-IFRS information, of this Annual Report.

4.1.4 Healthy people, sustainable planet

Sustainability continued to play an important role in the Personal Health businesses in 2017, with the main focus on optimizing the sustainability performance of our products and operations. Green Revenues – i.e. sales of products and solutions which meet or exceed our minimum requirements in the area of energy consumption, packaging and/or substances of concern – accounted for 58% of total sales in 2017. All Green Products with rechargeable batteries exceed the stringent California energy efficiency standard by at least 10%. And over 70% of total consumer sales are PVC- and/or BFR-free products (excluding power cords).

As part of our Circular Economy program we have continued to increase the use of recycled materials in our products. Over 1,850 tons of recycled plastics were used in kitchen appliances, vacuum cleaners, irons, air purification and coffee machines, compared to 1,440 tons in 2016. The revenue from Circular Products reached over EUR 473 million in 2017, comprised of turnover generated from performance- and access-based business models in Sleep & Respiratory Care and products with recycled plastic materials. Furthermore, circular opportunities across multiple products have been explored through pilots with access-based business models, which have the potential to generate future circular revenues. To maximize the use of resources and capture value from our commercial returns, pilots are running to sell refurbished products to our consumers – at the same time, capabilities are also being developed to enable the scale-up of these pilots.

As a concrete example of our commitment to sustainability we have improved the design of the 2000 Series Air Cleaner to ensure it meets the green product requirements. This means that the device meets the Chinese requirements for high cleaning energy efficiency, is free of polyvinylchloride (except power cord) and has over 600 grams of recycled plastics in the interior parts of the product.

In our operations, we continue to make positive progress towards our ultimate aim of having carbon-neutral production sites by 2020. In 2017, 47% of the electricity used in manufacturing sites came from renewable sources and 85% of the industrial waste was recycled. We sent 6% of our manufacturing waste to landfill in 2017. At the end of 2017, 9 out of 18 Personal Health businesses' manufacturing sites reported zero waste to landfill, with five achieving this status during the year. Based on detailed action plans we are working closely with the remaining sites to achieve zero waste to landfill status by the end of 2020.

4.2 Diagnosis & Treatment businesses

The Chief Business Leader of the Diagnosis & Treatment businesses segment, Rob Cascella, joined Philips in April 2015. He has more than 30 years of experience in the healthcare industry and has served on the boards of several companies, including 10 years as President and later CEO of Hologic Inc.

4.2.1 About Diagnosis & Treatment businesses

Our Diagnosis & Treatment businesses are foundational to our health technology strategy, delivering on the promise of precision medicine and least-invasive treatment and therapy. We enable our customers to realize the full potential of their 'quadruple aim' – to improve outcomes, lower the cost of care delivery and enhance patient and staff experiences – by enabling first-time-right diagnosis and treatment. We are focused on solutions (consisting of suites of systems, smart devices, software and services) that are robust and easy to use, while providing the most efficient path to obtaining a definitive diagnosis by integrating multiple sources of information and combining the data to create a comprehensive patient view. By bringing together imaging morphology, pathology and genomics, we are able to interrogate and extract the information needed to offer highly personalized care. Informatics is central to everything we do: our KLAS-awarded IntelliSpace Portal platform, for example, provides artificial intelligence to make more consistent decisions, as well as making it easier to share and collaborate.

We are expanding the applications for image-guided treatment and therapy – where clinicians are provided with the technology necessary to determine the presence of disease, guide procedures, deliver least-invasive treatment, and confirm effectiveness. Our solutions enable patient-specific treatment planning and selection, simplify complex procedures through integrated real-time guidance, and provide clinically proven treatment solutions. In 2017, we reinforced our leadership in image-guided therapy solutions with the global launch of Philips Azurion, the next-generation image-guided therapy platform that enables clinicians to perform a wide range of routine and complex procedures, helping them to optimize interventional lab performance and provide superior care. We provide image guidance both in our proprietary products and by partnering with radiation therapy companies like Elekta and IBA to deliver real-time, precise cancer treatment.

In 2017, Philips made two significant acquisitions to further strengthen our Diagnosis & Treatment businesses. Spectranetics' portfolio – including laser atherectomy catheters, the AngioSculptX drug-coated scoring balloon and the Stellarex drug-coated balloon – is highly complementary to Philips' and will support our expansion in image-guided therapy devices – specifically addressing peripheral vascular disease. Furthermore, to reinforce our leadership position in

ultrasound, Philips acquired TomTec Imaging Systems, a leading provider of clinical applications and intelligent image-analysis software.

In addition to our solutions for disease-specific clinical pathways, we provide a range of technologies to help our customers improve their operations and workflow. In 2017 we continued to build out our comprehensive PerformanceBridge suite of software services designed to improve radiology department operations, e.g. by providing practice management, dose management and service analytics. And we received FDA clearance for IntelliSpace Portal 9.0 and a range of innovative applications for radiology. The platform gives clinicians a comprehensive view of each patient, enabling efficient diagnosis of a broad range of conditions.

Our Diagnosis & Treatment businesses' value proposition to customers is based on leveraging our extensive clinical experience with our broad portfolio of technologies – making us uniquely capable to provide meaningful solutions that ultimately can improve the lives of the patients we serve while lowering the cost of care delivery for our customers.

Through our various businesses, Diagnosis & Treatment is focused on growing market share and profitability by:

- driving operational excellence in Diagnostic Imaging by delivering integrated products that are robust in design, easy to use, and promote efficient workflow
- enhancing our offerings in oncology, cardiology and radiology and expanding our solutions offering, which comprises systems, smart devices, software and services
- leveraging the Volcano and Spectranetics acquisitions and driving expansion into devices for treatment
- addressing underpenetrated adjacencies in general imaging and obstetrics/gynecology in Ultrasound, as well as expanding in point-of-care with new products and our partnership with B.Braun to innovate and accelerate growth in ultrasound-guided regional anesthesia and vascular access.

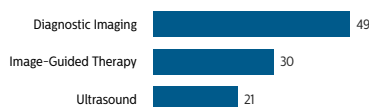
Philips is one of the world's leading health technology companies (based on sales) along with Medtronic, General Electric and Siemens. The competitive landscape in the healthcare industry is evolving with the emergence of new market players. The United States, our largest market, represented 34% of Diagnosis & Treatment's global sales in 2017, followed by China, Japan and Germany. Growth geographies accounted for 34% of Diagnosis & Treatment's sales. In 2017, Diagnosis & Treatment had 25,757 employees worldwide.

Through 2017 we consistently focused on our value-creation strategy to ensure continued growth and margin improvement.

In 2017, the Diagnosis & Treatment segment consisted of the following areas of business:

- **Diagnostic Imaging:** Magnetic Resonance Imaging, Computed Tomography, Advanced Molecular Imaging, Diagnostic X-Ray, which includes digital X-ray and mammography, and integrated clinical solutions, which include radiation oncology treatment planning, disease-specific oncology solutions and X-Ray dose management
- **Image-Guided Therapy:** interventional X-ray systems, encompassing cardiology, radiology and surgery, and interventional imaging and therapy devices that include Intravascular Ultrasound (IVUS), Fractional Flow Reserve (FFR) and atherectomy catheters and drug-coated balloons for the treatment of coronary artery and peripheral vascular disease
- **Ultrasound:** imaging products focused on diagnosis, treatment planning and guidance for cardiology, general imaging, obstetrics/gynecology, and point-of-care applications, as well as proprietary software capabilities to enable advanced diagnostics and intervention.

Diagnosis & Treatment
Total sales by business as a %
2017



Sales at Philips' Diagnosis & Treatment businesses are generally higher in the second half of the year, largely due to the timing of new product availability and customer spending patterns.

Sales channels are a mix of a direct sales force, especially in all the larger markets, combined with online sales portal and distributors – this varies by product, market and price segment. Sales are mostly driven by a direct sales force that has an intimate knowledge of the procedures for which our devices are used, and visits our customer base frequently.

Philips' Diagnosis & Treatment businesses are committed to compliance with regulatory product approval and quality system requirements in every market we serve, by addressing specific requirements of local and national regulatory authorities including the US FDA, the CFDA in China and comparable agencies in other countries, as well as the European Union's Waste from Electrical and Electronic Equipment (WEEE), Restriction of Hazardous

Substances (RoHS) and Registration, Evaluation, Authorization and Restriction of Chemicals (REACH) regulations.

The imaging businesses and image processing applications are governed by regulatory approvals in the markets that we serve. In almost all cases, new products that we introduce are subject to a regulatory approval process (e.g. 510k for FDA approvals in the USA). Failing to comply with the regulatory requirements can have severe consequences. The number and diversity of regulatory bodies in the various markets we operate in globally adds complexity and time to product introductions. Regulatory approval is a prerequisite for market introduction of medical devices.

With regard to the US Food and Drug Administration (FDA) inspection of the Cleveland facility (Illinois, USA) and Philips' Management System improvement program, please refer to [section 3.4, Our commitment to Quality](#), of this Annual Report.

With regard to sourcing, please refer to [sub-section 13.3.9, Supplier indicators](#), of this Annual Report.

4.2.2 2017 business highlights

Philips reinforced its leadership in image-guided therapy solutions with the global launch of Philips Azurion, the next-generation image-guided therapy platform that enables clinicians to perform a wide range of routine and complex procedures, helping them to optimize interventional lab performance and provide superior care.

To further strengthen its Diagnosis & Treatment businesses, Philips acquired Spectranetics. Its highly complementary portfolio, including laser atherectomy catheters, the AngioSculptX drug-coated scoring balloon and the Stellarex drug-coated balloon, will support Philips' expansion in image-guided therapy devices. Furthermore, to reinforce its leadership position in ultrasound, Philips acquired TomTec Imaging Systems, a leading provider of clinical applications and intelligent image-analysis software.

Philips Volcano continued its strong performance as the business reached an important milestone with the results of two large clinical trials demonstrating the benefits of Philips' Instant Wave-Free Ratio (iFR) technology compared to Fractional Flow Reserve (FFR), the current standard, removing a critical barrier for the use and adoption of iFR to decide, guide and confirm appropriate therapies.

B. Braun and Philips entered into a strategic alliance to innovate and accelerate growth in ultrasound-guided regional anesthesia and vascular access. The alliance launched Xperius, a new co-branded mobile ultrasound system specifically designed as the platform to support current and future integrated solutions in this fast-growing market.

Further strengthening its portfolio of imaging solutions, Philips received FDA 510(k) clearance for its ElastQ ultrasound imaging technology for non-invasive assessment of liver conditions. Philips also launched Access CT, a new CT system designed for healthcare organizations seeking to establish or enhance CT imaging capabilities at affordable cost.

Building on its portfolio of long-term strategic partnerships, Philips signed multiple new agreements. For example, Philips has partnered with the Singapore Institute of Advanced Medicine Holdings to provide its new oncology center with a range of Philips' advanced diagnostic imaging systems, combined with clinical informatics and services for a multi-year term.

Philips continued its strong growth momentum in China, driven by its innovative consumer health and professional healthcare portfolio, focused initiatives to step up market share and customer partnerships. This is illustrated by the double-digit growth in Diagnostic Imaging order intake¹⁾, which was in part driven by the strong traction in the private hospital segment, such as the new strategic partnership with Health 100, the largest health examination organization in China.

Driving its expansion in the fast-growing Obstetrics and Gynecology segment, Philips introduced new OB/GYN ultrasound innovations that are designed to support earlier, easier and more confident diagnoses. Highlighted features include anatomical-intelligence clinical decision support and workflow enhancements such as fingertip control and enhanced imaging versatility.

As part of Philips' new introductions to drive growth in diagnostic imaging, the company launched its digital MR Prodiva 1.5T system, which provides enhanced clinical performance and increased productivity, and introduced the latest configuration of its IQon Spectral CT, which is optimized to support the needs of emergency and oncology care. Moreover, since the third quarter of 2017, Philips has been shipping Vereos, the world's first and only fully digital PET/CT system, which is achieving market success due to its superb resolution, accuracy and efficiency.

Philips strengthened its Radiology Solutions offering with the acquisition of Analytical Informatics. Their suite of workflow improvement applications complements Philips' PerformanceBridge Practice to enable imaging departments to make data-driven improvement decisions. For example, Philips and Banner Health extended their partnership to include adoption of Philips' PerformanceBridge Practice across Banner's 28 radiology departments.

4.2.3 Financial performance

Net income is not allocated to segments as certain income and expense line items are monitored on a centralized basis.

Diagnosis & Treatment
Key data in millions of EUR unless otherwise stated
2015 – 2017

	2015	2016	2017
Sales	6,484	6,686	6,891
Sales growth			
Nominal sales growth	23%	3%	3%
Comparable sales growth ¹⁾	6%	4%	3%
Income from operations	322	546	488
as a % of sales	5.0%	8.2%	7.1%
Adjusted EBITA ¹⁾	515	631	716
as a % of sales	7.9%	9.4%	10.4%

In 2017, sales amounted to EUR 6,891 million, 3% higher than in 2016 on a nominal basis. Excluding a 1% negative currency effect, comparable sales¹⁾ increased by 3%, driven by mid-single-digit growth in Ultrasound and Image-Guided Therapy and low-single-digit growth in Diagnostic Imaging. Green Revenues amounted to EUR 5,096 million, or 74% of total segment sales.

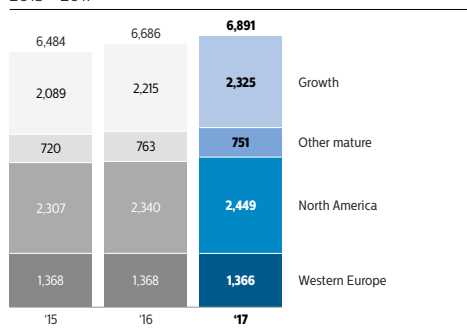
From a geographic perspective, nominal sales increased by 5% in growth geographies and on comparable sales¹⁾ showed high-single-digit growth, mainly driven by double-digit growth in China and high-single-digit growth in Latin America. Sales in mature geographies showed a 2% increase on a nominal basis and on a comparable basis recorded low-single-digit-growth, reflecting low-single-digit growth in North America and other mature geographies, while sales in Western Europe were flat year-on-year.

Income from operations decreased to EUR 488 million, or 7.1% of sales, compared to EUR 546 million, or 8.2% of sales, in 2016. The year 2017 included EUR 55 million of amortization charges, mainly related to intangible assets in Image-Guided Therapy compared to 2016, which included EUR 48 million of amortization charges, mainly related to acquired intangible assets in Image-Guided Therapy. Restructuring and acquisition-related charges were EUR 151 million, compared to EUR 37 million in 2016. The year 2017 also included charges of EUR 22 million related to portfolio rationalization measures.

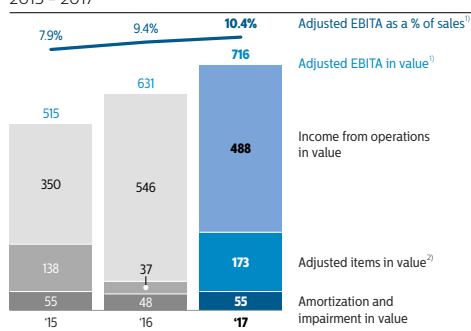
Adjusted EBITA¹⁾ increased by EUR 85 million or 100 basis points as a % of sales year-on-year. The increase was mainly attributable to higher volumes.

¹⁾ Non-IFRS financial measure. For the definition and reconciliation to the most directly comparable IFRS measure, refer to chapter 5, Reconciliation of non-IFRS information, of this Annual Report.

Diagnosis & Treatment
Sales per geographic cluster in millions of EUR
2015 – 2017



Diagnosis & Treatment
Income from operations and Adjusted EBITA¹⁾
in millions of EUR unless otherwise stated
2015 – 2017



¹⁾ Non-IFRS financial measure. For the definition and reconciliation to the most directly comparable IFRS measure, refer to [chapter 5, Reconciliation of non-IFRS information](#), of this Annual Report.

²⁾ Adjusted items include restructuring, acquisition-related and other charges

4.2.4 Healthy people, sustainable planet

Sustainability continued to play an important role in the Diagnosis & Treatment businesses in 2017. Philips continues to improve lives around the globe by developing diagnosis and treatment solutions that enable first-time-right diagnosis, precision interventions and therapy, while respecting the boundaries of natural resources.

In 2017, Green Revenues in Diagnosis & Treatment amounted to EUR 5,096 million, thanks to a large portfolio of Philips Green Products and Solutions that support energy efficiency, materials reduction and other sustainability goals. Philips actively collaborates with care providers around the globe to look for ways to minimize the environmental impact of healthcare. In a project together with Rijnstate Hospital in Arnhem (Netherlands), Philips has calculated that this hospital is saving about 64,000 kWh of electricity annually simply by powering-off imaging systems after hours. Philips has received third-party confirmation from COCIR that we are the frontrunner in MRI energy efficiency according to the COCIR SRI methodology and that our performance is 30% better than the industry average.

Supporting the transition to a circular economy, we have continued to expand the Diamond Select refurbishment program, spare parts recovery and SmartPath upgrading program for all modalities in the Diagnosis & Treatment portfolio. Philips is committed to 'closing the loop' on all large medical imaging equipment that becomes available to us. This means that we will actively pursue the trade-in of equipment such as MRI, CT and cardiovascular systems and we will take full control to ensure that all traded-in materials are repurposed in a responsible way. We plan to continue to expand these practices until we have covered all professional healthcare equipment.

Also in our operations we continue to make positive progress towards a circular economy by recycling 71% of our industrial waste. At the end of 2017, 5 out of 15 Diagnosis & Treatment businesses' manufacturing sites reported zero waste to landfill. Based on detailed action plans we are working closely with the remaining sites to achieve zero waste to landfill status by the end of 2020.

4.3 Connected Care & Health Informatics businesses

Dr. Carla Kriwet is Chief Business Leader of the Connected Care & Health Informatics businesses segment. She was appointed to this role in February 2017, succeeding Jeroen Tas. Prior to assuming her current role, Carla led Philips' Patient Care & Monitoring Solutions business group and was the Philips Market Leader of Germany, Austria & Switzerland. Before this, she held leadership positions with ABB Daimler Benz, The Boston Consulting Group, Linde AG and Draegerwerk in Europe and Asia. Carla is also Vice-Chairperson of Zeiss Meditec AG.

4.3.1 About Connected Care & Health Informatics businesses

Spanning the entire health continuum, the Connected Care & Health Informatics businesses aim to improve patient outcomes, increase efficiency and drive toward value-based care. Our solutions build on Philips' strength in patient monitoring and clinical informatics to improve clinical and economic outcomes in all care settings, within and outside the hospital.

Philips has a deep understanding of clinical care and the patient experience that, when coupled with our consultative approach, allows us to be an effective partner for transformation, both across the enterprise and at the level of the individual clinician. Philips delivers services that take the burden off hospital staff with a smooth integration process, improved workflow, customized training and improved accessibility across our application landscape.

This requires a common digital platform that connects and aligns consumers, patients, payers and healthcare providers. Philips' platforms aggregate and leverage information from clinical, personal and historical data to support care providers in delivering first-time-right diagnoses and treatment. Philips continually builds out new capabilities within Philips HealthSuite – a cloud-based connected health ecosystem of devices, apps and digital tools – to accomplish just that.

Philips delivers personalized insights by applying predictive analytics and artificial intelligence across our solutions. As an example, we are able to support healthcare professionals caring for elderly patients living independently at home in making clinical decisions and alerting medical teams to potential problems. Our integrated and data-driven approach promotes seamless patient care, helps identify risks and needs of different groups within a population, and provides clinical decision support.

In 2017, the Connected Care & Health Informatics segment consisted of the following areas of business:

- **Patient Care & Monitoring Solutions:** Enterprise-wide patient monitoring solutions, from value solutions to sophisticated solutions, for real-time clinical information at the patient's bedside; patient analytics, patient monitoring and clinical decision

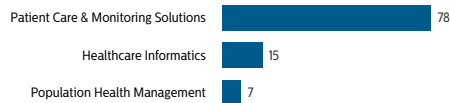
support systems, including diagnostic ECG data management for improved quality of cardiac care; therapeutic care, including cardiac resuscitation, emergency care solutions, invasive and non-invasive ventilators for acute and sub-acute hospital environments and respiratory monitoring devices; consumables across the patient monitoring and therapeutic care businesses; customer service, including clinical, IT, technical and remote customer propositions.

Effective 2018, Patient Care & Monitoring Solutions will transition into two focused business groups – Monitoring & Analytics and Therapeutic Care – to allow us to better fulfill the specific customer needs of each business.

- **Healthcare Informatics:** Advanced healthcare IT, clinical and advanced visualization and quantification informatics solutions for radiology, cardiology and oncology departments; Universal Data Management solutions, Picture Archiving and Communication Systems (PACS) and fully integrated Electronic Medical Record (EMR) systems to support healthcare enterprises in optimizing health system performance; advanced clinical and hospital IT platforms which are leveraged across Philips. Our IntelliSpace Portal application platform is recognized as industry-leading by KLAS. Today, with the role of the hospital CIO as a key decision maker increasing, integrated informatics solutions address challenges across the enterprise. We use artificial intelligence at the point of care to optimize the clinician experience, help improve productivity and total cost of ownership, and streamline patient experiences across the clinical pathway. Proof of clinical and economic outcomes, connectivity and cybersecurity are key priorities of our engagement with our customers.
- **Population Health Management:** Our services and solutions leverage data, analytics and actionable workflow products for solutions to improve clinical and financial results and increase patient engagement, satisfaction and compliance. These solutions include: technology-enabled monitoring and intervention (telehealth, remote patient monitoring, personal emergency response systems and care coordination) to improve the experience of elderly people and those living with chronic conditions; actionable programs to predict risk (including medication and care compliance, outreach, and fall prediction); cloud-based solutions for health organizations to manage population health. Leveraging the 2016 acquisition of Wellcentive, a leading US-based provider of population health management software solutions, our solutions enable health systems to analyze their patient population along clinical and financial criteria, coordinate care outside the hospital, and

engage patients in their health. They help drive quality improvement and business transformation for those transitioning to value-based care.

Connected Care & Health Informatics
Total sales by business as a %
2017



In 2017, Connected Care & Health Informatics had 10,949 employees worldwide.

Sales at Philips' Connected Care & Health Informatics businesses are generally higher in the second half of the year, largely due to customer spending patterns.

Sales channels include a mix of a direct salesforce (especially in larger markets), paired with an online sales portal and distributors (varying by product, market and price segment). Sales are mostly driven by a direct salesforce with an intimate knowledge of the procedures that use our integrated solutions' smart devices, systems, software and services. Philips works with customers and partners to co-create solutions, drive commercial innovation and adapt to new models like monitoring-as-a-service, outcome-based models (pay based on clinical and economical outcomes) and provider market models allowing providers to provide prices for episodes of care.

Philips' Connected Care & Health Informatics businesses are committed to compliance with regulatory product approval and quality system requirements in every market we serve, by addressing specific requirements of local and national regulatory authorities including the US FDA, the CFDA in China and comparable agencies in other countries, as well as the European Union's Waste from Electrical and Electronic Equipment (WEEE), Restriction of Hazardous Substances (RoHS) and Registration, Evaluation, Authorization and Restriction of Chemicals (REACH) regulations.

The connected care and health informatics applications are governed by regulatory approvals in the markets that we serve. In almost all cases, new products that we introduce are subject to a regulatory approval process (e.g. 510k for FDA approvals in USA, CE Mark in the European Union). Failing to comply with the regulatory requirements of the target markets can prevent shipment of products. The number and diversity of regulatory bodies in the various markets we operate in globally adds complexity and time to product introductions. Regulatory approval is a prerequisite for market introduction.

With regard to the consent decree agreed to by Philips and the US government, as announced in Philips' press release on October 11, 2017, please refer to [section 3.4, Our commitment to Quality](#), of this Annual Report

With regard to sourcing, please refer to [sub-section 13.3.9, Supplier indicators](#), of this Annual Report.

4.3.2 2017 business highlights

Demonstrating the success of telehealth technologies, Emory Healthcare (US) achieved savings of USD 4.6 million over a period of 15 months by using Philips' eICU platform. Similarly, with the help of Philips' Intensive Ambulatory Care program, Banner Health (US) reduced hospitalizations for chronically ill patients with multiple conditions by nearly 50%, reducing overall cost of care by more than one third.

Expanding its health informatics portfolio, Philips launched its IntelliSpace Enterprise Edition, an industry-first managed service solution for hospital-wide clinical informatics and data management. The high-performance, secure and scalable health informatics platform enables health systems to manage the growth and cost of their clinical enterprise with a pay-per-use model.

In line with Philips' focus on solutions selling, the company signed several multi-year agreements. For example, in Italy Philips signed a long-term strategic partnership agreement with the San Giovanni Calibita Fatebenefratelli Hospital in Rome to provide medical technologies, clinical informatics and services for state-of-the-art mother and child care. In the US, Philips expanded its relationship with Advocate Health Care, the largest health system in Illinois, to assist them in standardizing their clinical IT and patient monitoring solutions across the enterprise for improved patient outcomes and predictable costs. Furthermore, Philips signed an agreement with Lakeland Health in the US for advanced monitoring of patients in the hospital's general ward with the Philips IntelliVue Guardian Solution with Early Warning Scoring.

Demonstrating further progress on advanced data analytics, Philips received FDA clearance for its IntelliSpace Portal 10 and a range of innovative applications for radiology. The platform gives clinicians a comprehensive view of each patient, helping them to diagnose conditions. Further highlighting its leadership in health informatics, Philips signed several multi-year agreements with hospitals in the US to provide them with enterprise imaging informatics solutions.

Philips signed a new 10-year Managed Equipment Services agreement for patient monitoring solutions with Le Confluent, one of the top three private hospitals in France for cardiovascular care.

Expanding its health informatics portfolio, Philips acquired interoperability provider Forcare in the Netherlands. Philips also partnered with US-based

Nuance to bring Artificial Intelligence into radiology reporting by leveraging functionalities from Philips' Illumeo and Nuance's PowerScribe 360. Furthermore, Philips launched its new IntelliSpace Enterprise Edition for Radiology, providing radiology departments with comprehensive tools to increase efficiency and enhance throughput.

To further expand its Population Health Management business, Philips acquired VitalHealth, whose highly complementary portfolio of advanced analytics, care coordination, patient engagement and outcome management solutions will support Philips' commitment to deliver integrated solutions for care providers.

4.3.3 Financial performance

Net income is not allocated to segments as certain income and expense line items are monitored on a centralized basis.

Connected Care & Health Informatics
Key data in millions of EUR unless otherwise stated
2015 – 2017

	2015	2016	2017
Sales	3,022	3,158	3,163
Sales growth			
Nominal sales growth	13%	5%	0%
Comparable sales growth ¹⁾	0%	4%	3%
Income from operations	173	275	206
as a % of sales	5.7%	8.7%	6.5%
Adjusted EBITA ¹⁾	294	324	372
as a % of sales	9.7%	10.3%	11.8%

In 2017, sales amounted to EUR 3,163 million and remained flat compared with 2016 on a nominal basis. The 3% increase on a comparable basis¹⁾ was driven by mid-single-digit growth in Patient Care & Monitoring Solutions and low-single-digit growth in Healthcare Informatics. Green Revenues amounted to EUR 1,373 million, or 43% of segment sales.

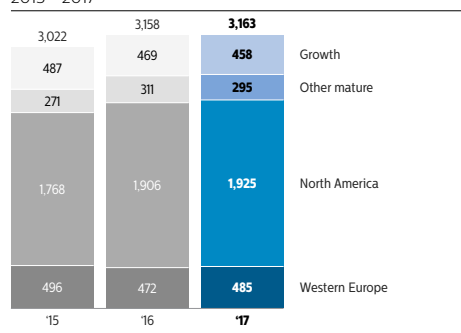
From a geographic perspective, sales on a nominal basis decreased by 2% in growth geographies; on a comparable basis sales¹⁾ showed low-single-digit growth, mainly driven by low-single-digit growth in China. Sales in mature geographies increased by 1% on a nominal basis and showed low-single-digit growth on a comparable basis, driven by mid-single-digit growth in Western Europe and North America, partly offset by a low-single-digit decline in other mature geographies.

Income from operations in 2017 decreased to EUR 206 million compared to EUR 275 million in 2016. The year 2017 included EUR 44 million of amortization charges, mainly related to acquired intangible assets in Population Health Management compared to 2016 which included EUR 46 million of amortization charges, mainly related to acquired intangible assets at Population Health Management and Patient Care &

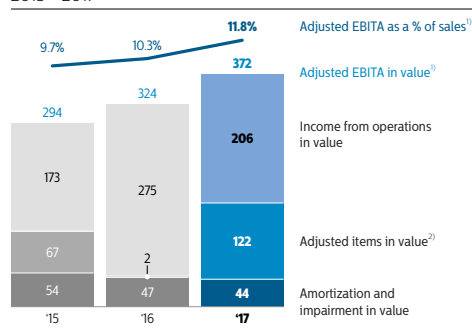
Monitoring Solutions. Restructuring and acquisition-related charges amounted to EUR 91 million compared to EUR 14 million in 2016. The year 2017 also included EUR 47 million of charges related to quality and regulatory actions, EUR 20 million of charges related to the consent decree focused on the defibrillator manufacturing in the US and a EUR 36 million net release of provisions.

Adjusted EBITA¹⁾ improved by EUR 48 million or 150 basis points as a % of sales year-on-year, mainly due to higher volumes, procurement savings and other cost productivity.

Connected Care & Health Informatics
Sales per geographic cluster in millions of EUR
2015 – 2017



Connected Care & Health Informatics
Income from operations and Adjusted EBITA¹⁾
in millions of EUR unless otherwise stated
2015 – 2017



¹⁾ Non-IFRS financial measure. For the definition and reconciliation to the most directly comparable IFRS measure, refer to chapter 5, Reconciliation of non-IFRS information, of this Annual Report

²⁾ Adjusted items include restructuring, acquisition-related and other charges

¹⁾ Non-IFRS financial measure. For the definition and reconciliation to the most directly comparable IFRS measure, refer to chapter 5, Reconciliation of non-IFRS information, of this Annual Report.

4.3.4 Healthy people, sustainable planet

Sustainability continued to play an important role in the Connected Care & Health Informatics businesses in 2017.

Green Revenues in Connected Care & Health Informatics amounted to EUR 1,373 million, 43% of total segment sales, with substantial contributions from all businesses. This reflects a continuous effort to improve energy efficiency, materials reductions and other green focus areas. With the growth of our software products and services and platform solutions, we are reducing our environmental footprint in a number of ways. For instance through software products that can replace hardware and the virtualization of servers. And indirectly through eHealth and connected care solutions that enable hospital workers to deliver faster, more personalized care while at the same time reducing transport to and from hospital.

In the transition towards a circular economy, we are actively pursuing innovations in design and business models that will help us 'close the loop'. This includes working together with customers and suppliers on improving takeback and upgrades of monitors. We are also working on closing loops for medical consumables and sensors, partly through partnerships with suppliers of refurbished materials. With our platform solutions like PACS and EMR, we continue to support fast, first-time-right diagnosis of patients, while at the same time helping hospitals to make efficient use of resources.

Also in our operations, we continue to make positive progress towards a circular economy by recycling 69% of our industrial waste. At the end of 2017, 3 out of 5 Connected Care & Health Informatics businesses' manufacturing sites reported zero waste to landfill. Based on detailed action plans we are working closely with the remaining sites to achieve zero waste to landfill status by the end of 2020.

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4.4 HealthTech Other

In our external reporting on HealthTech Other we report on the items Innovation, Emerging Businesses, IP Royalties, Central costs and Other.

4.4.1 About HealthTech Other

Innovation & Strategy

The central Innovation & Strategy organization includes, among others, the Chief Technology Office, Research, Digital Platforms, the Chief Medical Office, Innovation Services, Design, Strategy, and Sustainability. Key locations include Eindhoven (Netherlands), Cambridge (USA), Bangalore (India) and Shanghai (China).

Innovation & Strategy is responsible for collaborating with the operating businesses and the markets to continuously update the company strategy, in line with our growth and profitability ambitions, in the context of the changing competitive landscape and market trends, while fully leveraging Philips' capabilities, assets and positions.

Innovation & Strategy facilitates innovation from idea to market as co-creator and strategic partner for the Philips businesses and complementary partners. It does so through cooperation between research, design, marketing, strategy and businesses in interdisciplinary teams along the innovation chain, from front-end to first-of-a-kind proposition development. In addition, it opens up new value spaces beyond the direct scope of current businesses, manages the Company-funded R&D portfolio, and creates synergies for cross-segment initiatives and integrated solutions.

Innovation & Strategy actively participates in Open Innovation through relationships with academic, clinical, industrial partners and start-ups, as well as via public-private partnerships. It does so in order to improve innovation effectiveness and efficiency, capture and generate new ideas, enhance technology partnering capabilities, and share the related financial exposure.

Finally, Innovation & Strategy also has the functional responsibility for R&D, Innovation, Design, Medical Affairs, and Sustainability, with representatives or teams embedded in the business groups. Innovation & Strategy sets the agenda and drives continuous improvement in the efficiency and effectiveness of innovation, as well as the creation and adoption of digital platforms, and the uptake of new technologies such as data science and artificial intelligence.

The CTO organization

The CTO organization is an integrated group of innovation organizations that plays a strong role in orchestrating innovation across Philips' businesses and markets, as well as initiating game-changing innovation that disrupts and crosses boundaries in health technology.

The CTO organization includes the following organizations:

- **Innovation Management**, responsible for end-to-end innovation strategy and portfolio management, integrated roadmaps linked to solutions and our designated 'health spaces', the common components strategy, R&D competency management, innovation performance management and public funding programs.
- **Philips Research**, the co-creator and strategic partner of the Philips businesses, markets and complementary open innovation ecosystem participants driving front-end innovation.
- **The Clinical Research Board**, responsible for managing key global academic accounts and positioning Philips as a leading partner for clinical research.
- **The Chief Architect Office**, responsible for defining, steering and ensuring compliance and uptake of the Philips Unified Architecture, software harmonization and standards.
- **Philips HealthWorks**, responsible for de-risking and accelerating breakthrough innovation and for driving a mindset change towards a more entrepreneurial and open innovation culture. HealthWorks incubates early-stage ventures and engages with the external start-up ecosystem.
- **HealthSuite Insights**, our data science and artificial intelligence platform and entrepreneurial team, offering a consistent set of tools, technologies, and proprietary clinical assets for data scientists and development teams to use in analyzing their data. Our customers can leverage existing assets, or build and host new assets on Philips' infrastructure as part of our data science marketplace.

One of the ventures reporting into the Chief Technology Office is **Philips Photonics**, a global leader in VCSEL technology. VCSELs are infrared lasers for a rapidly growing range of consumer and professional applications like gesture control, environmental sensing, precise scene illumination for surveillance cameras and ultra-fast data communication.

Philips HealthSuite Digital Platforms

The Philips HealthSuite Digital Platforms are our common digital framework that connects consumers, patients and healthcare providers in a cloud-based connected health ecosystem of devices, apps and tools.

- **HealthSuite Cloud** allows Philips and our partners to create the next generation of connected health and wellness innovations from a clinical and technical perspective.
- **HealthSuite Premise** enables our customers to host their own data, control the flow of information between their own systems and the cloud, and still benefit from the digital capabilities that we have to offer.

- **HealthSuite Insights**, already mentioned above, is our data science and AI platform, which can also be deployed in the cloud or on-premise.
- **HealthSuite Consumer Engagement** is our platform for reusable components across our consumer and IoT (Internet of Things) landscape. A common architecture not only enables shorter development times and lower costs – it also enables seamless interoperability across businesses and propositions, creating stronger and more unique value propositions.
- **HealthSuite Clinical Platform** provides a consistent clinical user experience across enterprise, diagnostic imaging and interventional systems.

The Philips HealthSuite Digital Platforms are managed and orchestrated across Innovation & Strategy and all Philips businesses.

Chief Medical Office

The Chief Medical Office is responsible for clinical innovation and strategy, health economics and market access, and medical thought leadership. This includes engaging with stakeholders across the care continuum to extend Philips' leadership in health technology and acting with agility on new value-based reimbursement models that benefit the patient and care provider.

Leveraging the knowledge and expertise of the medical professional community across Philips, the Chief Medical Office includes many healthcare professionals who practice in the world's leading health systems. Supporting the company's objectives across the health continuum, its activities include strategic guidance, leveraging clinical and scientific knowledge, fostering peer-to-peer relationships in relevant medical communities, liaising with medical regulatory bodies, and supporting clinical and marketing evidence development.

Philips Design

Philips Design is the global design function for the company, ensuring that innovations are meaningful, people-focused and locally relevant. Design is also responsible for ensuring that the Philips brand experience is differentiating, consistently expressed, and drives customer preference.

Philips Design partners with stakeholders across the organization to develop methodologies and enablers to define value propositions, implement data-enabled design tools and processes to create meaning from data and leverage Cocreate methodologies to define solutions with all key stakeholders. Our design-thinking Cocreate approach facilitates collaboration with customers and patients to create solutions that are tailored specifically to the challenges facing them today, as local circumstances and workflows are key ingredients in the successful implementation of solutions to the challenges our customers face.

To ensure that we connect end users along the health continuum we create a consistent experience across all touchpoints. A key enabler for this is a consistent and differentiating design language that applies to software, hardware and services across our operating businesses. In recognition of our continued excellence, Philips Design received 165 awards in 2017.

Innovation Services

Innovation Services offers a wide range of expert services in technology development, realization and industry consulting, ranging from mechatronics and systems engineering, to micro-electro mechanical systems and devices. Its skills are leveraged by Philips' businesses, markets and Innovation & Strategy in all regions.

Innovation Hubs

To ensure a critical mass of innovation capabilities that leverage the strengths of relevant innovation health technology ecosystems and that can optimally serve market-driven innovation as well as new business creation, we have established four Innovation Hubs for the Philips Group: Cambridge (US), Eindhoven (Netherlands), Bangalore (India) and Shanghai (China). Each Hub includes a combination of technical, design and clinical capabilities, representing Group Innovation & Strategy, selected R&D groups from our businesses, market innovation teams and other functions. These Hubs, where most of the Group Innovation & Strategy organization is concentrated, complement the business-specific innovation capabilities of our R&D centers that are integrated in our global business sites.

- **The Philips Innovation Center Eindhoven** is Philips' largest Innovation Hub worldwide, hosting the global headquarters of many of our innovation organizations.
- **The Philips Cambridge, MA, Innovation Labs** is home to both researchers and employees from other innovation functions and ventures. Being within close proximity to the MIT campus and clinical collaboration partners allows researchers to collaborate easily with MIT faculties and PhD students on jointly defined research programs, as well as to participate in Open Innovation projects.
- **The Philips Innovation Campus Bangalore** hosts activities from most of our operating businesses, Research, Design, IP&S and IT. R&D activities at the site include Diagnostic Imaging, Patient Care & Monitoring Solutions, Sleep & Respiratory Care, Personal Health, and Healthcare Informatics. The campus works with growth geographies to build market-specific solutions, and several businesses have also located business organizations focusing on growth geographies at the site.
- **The China Innovation Hub** in Shanghai combines digital innovation, research and solutions development capabilities responsible for developing locally and globally relevant innovations.

Alongside the hubs, where most of the central Innovation & Strategy organization is concentrated together with selected business R&D and market innovation teams, we continue to have significant, more focused innovation capabilities integrated into key technology centers at our global business sites.

Emerging Businesses

Emerging Businesses is a business group dedicated to a mission of bringing intelligence to advance diagnosis in pathology and neurology and to guide therapy. It includes, among others:

- **Digital & Computational Pathology** is focused on two key missions: to digitize diagnosis in anatomic pathology, and to use Artificial Intelligence to aid detection of disease and progression to reduce inter-observer variability and improve outcomes. Philips is the global market leader in routine primary diagnosis using Digital Pathology and the only company in the market to have an FDA-approved solution for primary diagnosis.
- **Philips Neuro** is focused on a mission to advance neuroscience for better care. The business provides an integrated neurology solution comprising Full Head HD EEG with diagnostic imaging to map brain activity and anatomy for a wide range of neuro disorders, and uses machine learning to improve diagnosis of various neuro disorders. In June 2017, Philips acquired Electrical Geodesics, Inc., a US-based company that designs, develops and commercializes a range of non-invasive technologies used to monitor and interpret brain activity.

IP Royalties

Philips Intellectual Property & Standards proactively pursues the creation of new Intellectual Property (IP) in close co-operation with Philips' operating businesses and Innovation & Strategy. IP&S is a leading industrial IP organization providing world-class IP solutions to Philips' businesses to support their growth, competitiveness and profitability.

Royal Philips' total IP portfolio currently consists of 62,000 patent rights, 37,600 trademarks, 47,800 design rights and 3,000 domain names. Philips filed 1,200 new patents in 2017, with a strong focus on the growth areas in health and well-being.

IP&S participates in the setting of standards to create new business opportunities for the Philips operating businesses. A substantial portion of revenue and costs is allocated to the operating businesses. Philips believes its business as a whole is not materially dependent on any particular patent or license, or any particular group of patents and licenses.

Central costs

The central cost organization supports the creation of value, connecting Philips with key stakeholders, especially our employees, customers, governments

and society. It includes the Executive Committee, Brand Management, Sustainability, New Venture Integration, the Group functions related to strategy, human resources, legal and finance, as well as country and regional management. It also includes functional services to businesses in areas such as IT, Real Estate and Accounting, thereby helping to drive global cost efficiencies.

4.4.2 2017 business highlights

Highlighting Philips' leadership in digital pathology, the Pathology Institute in Hall (Austria) and the Pathology Institute at Tirol Kliniken Innsbruck (Austria) fully digitized their diagnostic process with Philips' comprehensive IntelliSite Pathology Solution.

In the 2017 Interbrand annual ranking of the world's most valuable brands, Philips ranked #41 with an increased estimated brand value of USD 11.5 billion.

Philips' IntelliSite Pathology Solution is currently the only digital pathology solution in the US to receive FDA clearance for primary diagnostic use. This achievement reinforces Philips' leadership in digital pathology, a solution that is central to the diagnosis of complex diseases such as cancer.

Philips was named Industry Leader in the Diversified Industrials category in the 2017 Dow Jones Sustainability Index for the third year in a row, achieving best-in-class scores in several categories, including corporate governance, climate strategy and operational eco-efficiency.

Philips signed an agreement for a new EUR 1 billion Revolving Credit Facility with an interest rate that is dependent on the company's year-on-year improvement in its sustainability performance.

Philips was one of the signatories to the Dutch Gold Sector International Responsible Business Conduct (IRBC) Agreement, which aims to ensure greater respect for human rights, the environment and biodiversity throughout the chain, from mining to recycling.

4.4.3 Financial performance

Net income is not allocated to segments as certain income and expense line items are monitored on a centralized basis.

HealthTech Other
Key data in millions of EUR
2015 – 2017

	2015	2016	2017
Sales	503	478	415
Income from operations	49	(129)	(149)
Adjusted EBITA ¹⁾	8	(66)	(109)
IP Royalties	284	286	225
Innovation	(186)	(207)	(212)
Central costs	(83)	(137)	(105)
Other	(7)	(8)	(17)

¹⁾ Non-IFRS financial measure. For the definition and reconciliation to the most directly comparable IFRS measure, refer to [chapter 5, Reconciliation of non-IFRS information](#), of this Annual Report.

In 2017, sales amounted to EUR 415 million compared to EUR 478 million in 2016, mainly due to lower royalty income.

In 2017, Income from operations totaled to EUR (149) million compared to EUR (129) million in 2016. The year 2017 included restructuring and acquisition-related charges of EUR 64 million and a EUR 59 million net gain from the sale of real estate assets. The year 2016 included restructuring and acquisition-related charges of EUR 28 million and a EUR 26 million impairment of real estate assets. The year-on-year decrease was mainly due to lower royalty income, higher restructuring and acquisition-related charges and higher provision-related charges, partly offset by lower Central costs.

Adjusted EBITA¹⁾ decreased by EUR 43 million compared to 2016, mainly due to lower royalty income and higher provision-related charges in Other, partly offset by lower Central costs.

4.5 Legacy Items

Legacy Items consists mainly of separation costs, legacy legal items, legacy pension costs, environmental provisions and stranded costs.

4.5.1 Financial performance

Legacy Items
Key data in millions of EUR unless otherwise stated
2015 – 2017

	2015	2016	2017
Separation costs	(183)	(152)	(31)
Other	(439)	(29)	(73)
Income from operations	(622)	(181)	(103)

Income from operations in 2017 mainly included EUR 31 million of charges related to the separation of the Lighting business, EUR 26 million of provisions related to the CRT litigation in the US, EUR 15 million of costs related to environmental provisions, and EUR 14 million of stranded costs related to the combined Lumileds and Automotive businesses.

¹⁾ Non-IFRS financial measure. For the definition and reconciliation to the most directly comparable IFRS measure, refer to [chapter 5, Reconciliation of non-IFRS information](#), of this Annual Report.

5 Reconciliation of non-IFRS information

In this Annual Report Philips presents certain financial measures when discussing Philips' performance that are not measures of financial performance or liquidity under IFRS ('non-IFRS'). These non-IFRS measures (also known as non-GAAP or alternative performance measures) are presented because management considers them important supplemental measures of Philips' performance and believes that they are widely used in the industry in which Philips operates as a means of evaluating a company's operating performance and liquidity. Philips believes that an understanding of its sales performance, profitability, financial strength and funding requirements is enhanced by reporting the following non-IFRS measures:

- Comparable sales growth;
- Adjusted EBITA;
- Adjusted EBITDA;
- Free cash flow;
- Net debt : group equity ratio; and
- Comparable order intake.

Non-IFRS measures do not have standardized meanings under IFRS and not all companies calculate non-IFRS measures in the same manner or on a consistent basis. As a result, these measures (and ratios based on these measures) may not be comparable to measures used by other companies that have the same or similar names. Accordingly, undue reliance should not be placed on the non-IFRS measures contained in this Annual Report and they should not be considered as substitutes for sales, net income, net cash provided by operating activities or other financial measures computed in accordance with IFRS.

This chapter contains the definitions of the non-IFRS measures used in this Annual Report as well as reconciliations from the most directly comparable IFRS measures. The non-IFRS measures discussed in this Annual Report are cross referenced to this chapter. These non-IFRS measures should not be viewed in isolation or as alternatives to equivalent IFRS measures and should be used in conjunction with the most directly comparable IFRS measures.

The non-IFRS financial measures presented are not measures of financial performance or liquidity under IFRS, but measures used by management to monitor

the underlying performance of Philips' business and operations and, accordingly, they have not been audited or reviewed by Philips' external auditors. Furthermore, they may not be indicative of Philips' future results and should not be construed as an indication that Philips' future results will be unaffected by exceptional or non-recurring items.

Comparable sales growth

Comparable sales growth represents the period-on-period growth in sales excluding the effects of currency movements and changes in consolidation. As indicated in [note 1, Significant accounting policies](#), to the Philips Group financial statements, foreign currency sales and costs are translated into Philips' presentation currency, the euro, at the exchange rates prevailing at the respective transaction dates. As a result of significant foreign currency sales and currency movements during the periods presented, the effects of translating foreign currency sales amounts into euros could have a material impact on the comparability of sales between periods. Therefore, these impacts are excluded when presenting comparable sales in euros by translating the foreign currency sales of the previous period and the current period into euros at the same average exchange rates. In addition, the years under review were affected by a number of acquisitions and divestments, as a result of which various activities were consolidated or deconsolidated. The effect of consolidation changes has also been excluded in arriving at the comparable sales. For the purpose of calculating comparable sales, when a previously consolidated entity is sold or control is lost, relevant sales for that entity of the corresponding prior year period are excluded. Similarly, when an entity is acquired and consolidated, relevant sales for that entity of the current year period are excluded.

Comparable sales growth is presented for the Philips Group, operating segments and geographic clusters. Philips' believes that the presentation of comparable sales growth is meaningful for investors to evaluate the performance of Philips' business activities over time. Comparable sales growth may be subject to limitations as an analytical tool for investors, because comparable sales growth figures are not adjusted for other effects, such as increases or decreases in prices or quantity/volume. In addition, interaction effects between currency movements and changes in consolidation (second order effects) are not taken into account.

Philips Group
Sales growth composition per segment in %
 2015 – 2017

	nominal growth	currency effects	consolidation changes	comparable growth
2017 versus 2016				
Personal Health	3.0	1.9	0.7	5.6
Diagnosis & Treatment	3.1	2.0	(1.6)	3.5
Connected Care & Health Informatics	0.2	1.9	1.1	3.2
<i>HealthTech Other</i>	(13.2)	0.2	0.1	(12.9)
Philips Group	2.1	1.9	(0.1)	3.9

2016 versus 2015

Personal Health	5.2	2.0	0.0	7.2
Diagnosis & Treatment	3.1	0.9	(0.4)	3.6
Connected Care & Health Informatics	4.5	0.1	(0.1)	4.5
<i>HealthTech Other</i>	(5.0)	0.0	0.0	(5.0)
Philips Group	3.7	1.1	0.1	4.9

2015 versus 2014

Personal Health	13.5	(8.6)	0.0	4.9
Diagnosis & Treatment	22.7	(10.9)	(5.7)	6.1
Connected Care & Health Informatics	12.6	(12.2)	0.0	0.4
<i>HealthTech Other</i>	3.3	(0.3)	(1.9)	1.1
Philips Group	15.8	(9.9)	(1.5)	4.4

Philips Group
Sales growth composition per geographic cluster in %
 2015 – 2017

	nominal growth	currency effects	consolidation changes	comparable growth
2017 versus 2016				
Western Europe	1.2	1.1	0.5	2.8
North America	2.1	2.0	(1.4)	2.7
Other mature geographies	(4.7)	2.6	(0.1)	(2.2)
Mature geographies	0.8	1.7	(0.6)	1.9
Growth geographies	4.8	2.3	0.9	8.0
Philips Group	2.1	1.9	(0.1)	3.9

2016 versus 2015

Western Europe	2.2	1.9	0.2	4.3
North America	3.6	(0.4)	(0.2)	3.0
Other mature geographies	8.9	(6.2)	(0.4)	2.3
Mature geographies	3.9	(0.5)	(0.1)	3.3
Growth geographies	3.2	4.6	0.6	8.4
Philips Group	3.7	1.1	0.1	4.9

2015 versus 2014

Western Europe	6.3	(2.2)	(1.2)	2.9
North America	23.8	(18.8)	(2.6)	2.4
Other mature geographies	12.6	(5.4)	(4.2)	3.0
Mature geographies	16.0	(11.0)	(2.3)	2.7
Growth geographies	15.3	(7.3)	0.1	8.1
Philips Group	15.8	(1.5)	(9.9)	4.4

Adjusted EBITA

The term Adjusted EBITA is used to evaluate the performance of Philips and its segments. EBITA represents Income from operations excluding amortization and impairment of acquired intangible assets and impairment of goodwill. Adjusted EBITA represents EBITA excluding gains or losses from restructuring costs, acquisition-related charges and other items.

Restructuring costs are defined as the estimated costs of initiated reorganizations, the most significant of which have been approved by the Executive Committee, and which generally involve the realignment of certain parts of the industrial and commercial organization.

Acquisition-related charges are defined as costs that are directly triggered by the acquisition of a company, such as transaction costs, purchase accounting related costs and integration-related expenses.

Other items are defined as any individual item with an income statement impact (loss or gain) that is deemed by management to be both significant and incidental to normal business activity. Other items may extend over several quarters and are not limited to the same financial year.

Philips considers use of Adjusted EBITA appropriate as Philips uses it as a measure of segment performance and as one of its strategic drivers to increase profitability through re-allocation of its resources towards opportunities offering more consistent and higher returns. This is done with the aim of making the underlying performance of the businesses more transparent.

Philips believes Adjusted EBITA is useful to evaluate financial performance on a comparable basis over time by factoring out restructuring costs, acquisition-related charges and other incidental items which are not directly related to the operational performance of Philips Group or its segments.

Adjusted EBITA may be subject to limitations as an analytical tool for investors, as it excludes restructuring costs, acquisition-related charges and other incidental items and therefore does not reflect the expense associated with such items, which may be significant and have a significant effect on Philips' net income.

Adjusted EBITA margin refers to Adjusted EBITA divided by sales expressed as a percentage.

Adjusted EBITA is not a recognized measure of financial performance under IFRS. Below is a reconciliation of Adjusted EBITA to the most directly comparable IFRS measure, Net income, for the years indicated. Net income is not allocated to segments as certain income and expense line items are monitored on a centralized basis, resulting in them being shown on a Philips Group level only.

Philips Group

Reconciliation of Net income to Adjusted EBITA in millions of EUR unless otherwise stated
2015 – 2017

	Philips Group	Personal Health	Diagnosis & Treatment	Connected Care & Health Informatics	HealthTech Other	Legacy Items
2017						
Net Income	1,870					
Discontinued operations, net of income taxes	(843)					
Income tax expense	349					
Investments in associates, net of income taxes	4					
Financial expense	263					
Financial income	(126)					
Income from operations	1,517	1,075	488	206	(149)	(103)
Amortization of acquired intangible assets	260	135	55	44	26	
Impairment of goodwill	9				9	
EBITA	1,787	1,211	543	250	(114)	(103)
Restructuring and acquisition-related charges	316	11	151	91	64	
Other items	50		22	31	(59)	55
Adjusted EBITA	2,153	1,221	716	372	(109)	(48)
Sales	17,780	7,310	6,891	3,163	415	1
Adjusted EBITA as a % of sales	12.1%	16.7%	10.4%	11.8%		
2016						
Net Income	1,491					
Discontinued operations, net of income taxes	(660)					
Income tax expense	203					
Investments in associates, net of income taxes	(11)					
Financial expenses	507					
Financial income	(65)					
Income from operations	1,464	953	546	275	(129)	(181)
Amortization of acquired intangible assets	242	139	48	46	9	
Impairment of goodwill	1			1		
EBITA	1,707	1,092	594	322	(120)	(181)
Restructuring and acquisition-related charges	94	16	37	14	28	(1)
Other items	120			(12)	26	106
Adjusted EBITA	1,921	1,108	631	324	(66)	(76)
Sales	17,422	7,099	6,686	3,158	478	1
Adjusted EBITA as a % of sales	11.0%	15.6%	9.4%	10.3%		
2015						
Net Income	638					
Discontinued operations, net of income taxes	(479)					
Income tax expense	169					
Investments in associates, net of income taxes	(30)					
Financial expenses	453					
Financial income	(94)					
Income from operations	658	736	322	173	49	(622)
Amortization of acquired intangible assets	273	149	55	54	15	
EBITA	931	885	377	227	64	(622)
Restructuring and acquisition-related charges	186	37	131	38	(19)	(1)
Other items	571	44	7	29	(37)	528
Adjusted EBITA	1,688	966	515	294	8	(95)
Sales	16,806	6,751	6,484	3,022	503	46
Adjusted EBITA as a % of sales	10.0%	14.3%	7.9%	9.7%		

Adjusted EBITDA

Adjusted EBITDA is defined as Income from operations excluding amortization and impairment of intangible assets, impairment of goodwill, depreciation and impairment of property, plant and equipment, restructuring costs, acquisition-related charges and other items.

Philips understands that Adjusted EBITDA is broadly used by analysts, rating agencies and investors in their evaluation of different companies because it excludes certain items that can vary widely across different industries or among companies within the same industry. Philips considers Adjusted EBITDA useful when comparing its performance to other companies in the HealthTech industry. However, Adjusted EBITDA may be subject to limitations as an analytical tool because of the range of items excluded and their significance in a given reporting period. Furthermore, comparisons with other companies may be complicated due to the absence of a standardized meaning and calculation framework. Our management compensates for the limitations of using Adjusted EBITDA by using this measure to supplement IFRS results to provide a more complete understanding of the factors and trends affecting the business rather than IFRS results alone. In addition to the limitations noted above, Adjusted EBITDA excludes items that may be recurring in nature and should not be disregarded in the evaluation of performance. However, we believe it is useful to exclude such items to provide a supplemental analysis of current results and trends compared to other periods because certain excluded items can vary significantly depending on specific underlying transactions or events, and the variability of such items may not relate specifically to ongoing operating results or trends and certain excluded items, while potentially recurring in future periods, may not be indicative of future results. A reconciliation from net income to Adjusted EBITDA is provided below.

Philips Group
Reconciliation of Net income to Adjusted EBITDA in millions of EUR
 2015 – 2017

	Philips Group	Personal Health	Diagnosis & Treatment	Connected Care & Health Informatics	HealthTech Other	Legacy Items
2017						
Net income	1,870					
Discontinued operations, net of income taxes	(843)					
Income tax expense	349					
Investment in associates, net of income taxes	4					
Financial expense	263					
Financial income	(126)					
Income from operations	1,517	1,075	488	206	(149)	(103)
Depreciation, amortization and impairment of assets	1,025	371	267	208	177	2
Impairment of goodwill	9				9	
Restructuring costs	211	8	63	81	59	
Acquisition-related charges	106	3	88	10	5	
Other items	50		22	31	(59)	55
Adding back impairment of fixed assets included in restructuring and acquisition-related changes and other items	(86)	(1)	(44)	(34)	(7)	-
Adjusted EBITDA	2,832	1,456	884	502	36	(46)
2016						
Net income	1,491					
Discontinued operations, net of income taxes	(660)					
Income tax expense	203					
Investment in associates, net of income taxes	(11)					
Financial expense	507					
Financial income	(65)					
Income from operations	1,464	953	546	275	(129)	(181)
Depreciation, amortization and impairment of assets	976	385	229	184	177	2
Impairment of goodwill	1			1		
Restructuring costs	58	16	6	9	27	(1)
Acquisition-related charges	37		31	4	1	
Other items	120			(12)	26	106
Adding back impairment of fixed assets included in restructuring and acquisition-related changes and other items	(42)	-	(4)	(4)	(34)	
Adjusted EBITDA	2,613	1,353	808	458	68	(74)
2015						
Net income	638					
Discontinued operations, net of income taxes	(479)					
Income tax expense	169					
Investment in associates, net of income taxes	(30)					
Financial expense	453					
Financial income	(94)					
Income from operations	658	736	322	173	49	(622)
Depreciation, amortization and impairment of assets	972	375	249	198	156	(7)
Restructuring costs	81	38	25	37	(20)	(1)
Acquisition-related charges	107	(1)	107	1		
Other items	571	44	7	29	(37)	528
Adding back impairment of fixed assets included in restructuring and acquisition-related changes and other items	(80)	(4)	(62)	(14)		
Adjusted EBITDA	2,307	1,188	648	424	149	(102)

Free cash flow

Free cash flow is defined as net cash provided by operating activities minus net capital expenditures. Net capital expenditures are comprised of the purchase of intangible assets, expenditures on development assets, capital expenditures on property, plant and equipment and proceeds from sales of property, plant and equipment.

Philips discloses free cash flow as a supplemental non-IFRS financial measure, as Philips believes it is a meaningful measure to evaluate the performance of its business activities over time. Philips understands that free cash flow is broadly used by analysts, rating agencies and investors in assessing its performance. Philips also believes that the presentation of free cash flow provides useful information to investors regarding the cash generated by the Philips operations after deducting cash outflows for purchases of intangible assets, capitalization of product development, expenditures on development assets,

capital expenditures on property, plant and equipment and proceeds from disposal of property, plant and equipment. Therefore, the measure gives an indication of the long-term cash generating ability of the business. In addition, because free cash flow is not impacted by purchases or sales of businesses and investments, it is generally less volatile than the total of net cash provided by operating activities and net cash provided used for investing activities.

Free cash flow may be subject to limitations as an analytical tool for investors, as free cash flow is not a measure of cash generated by operations available exclusively for discretionary expenditures and Philips requires funds in addition to those required for capital expenditures for a wide variety of non-discretionary expenditures, such as payments on outstanding debt, dividend payments or other investing and financing activities. In addition, free cash flow does not reflect cash payments that may be required in future for costs already incurred, such as restructuring costs.

Philips Group
Composition of free cash flow in millions of EUR
2015 – 2017

	2015	2016	2017
Net cash provided by operating activities	598	1,170	1,870
Net capital expenditures	(752)	(741)	(685)
Purchase of intangible assets	(105)	(95)	(106)
Expenditures on development assets	(291)	(301)	(333)
Capital expenditures on property, plant and equipment	(432)	(360)	(420)
Proceeds from sales of property, plant and equipment	76	15	175
Free cash flow	(154)	429	1,185

Net debt : group equity ratio

Net debt : group equity ratio is presented to express the financial strength of Philips. Net debt is defined as the sum of long- and short-term debt minus cash and cash equivalents. Group equity is defined as the sum of shareholders' equity and non-controlling interests. This measure is used by Philips Treasury management and investment analysts to evaluate financial strength and

funding requirements. This measure may be subject to limitations because cash and cash equivalents are used for various purposes, not only debt repayment. The net debt calculation deducts all cash and cash equivalents whereas these items are not necessarily available exclusively for debt repayment at any given time.

Philips Group
Composition of net debt and group equity in millions of EUR unless otherwise stated
2015–2017

	2015	2016	2017
Long-term debt	4,095	4,021	4,044
Short-term debt	1,665	1,585	672
Total debt	5,760	5,606	4,715
Cash and cash equivalents	1,766	2,334	1,939
Net debt	3,994	3,272	2,776
Shareholders' equity	11,607	12,546	11,999
Non-controlling interest	118	907	24
Group equity	11,725	13,453	12,023
Net debt : group equity ratio	25:75	20:80	19:81

Comparable order intake

Comparable order intake is reported for equipment and software and is defined as the total contractually committed amount to be delivered within a specified timeframe excluding the effects of currency movements and changes in consolidation. Comparable order intake does not derive from the financial statements and thus a quantitative reconciliation is not provided.

Philips uses comparable order intake as an indicator of business activity and performance. Comparable order intake is not an alternative to revenue and may be subject to limitations as an analytical tool due to differences in amount and timing between booking orders and revenue recognition. Due to divergence in practice, other companies may calculate this or a similar measure (such as order backlog) differently and therefore comparisons between companies may be complicated.

6 Risk management

6.1 Our approach to risk management

The Executive Committee, supported by the Risk Management Support Team, oversees and manages risks associated with Philips' strategy and activities. The Risk Management Support Team consists of a number of functional experts covering the various categories of enterprise risk and supports by increasing the understanding of the enterprise risk profile and continuously working to improve the enterprise risk management framework. The Executive Committee is ultimately responsible for identifying the critical risks and for the implementation of appropriate risk responses. The Supervisory Board is periodically updated about enterprise risks and the risk management process in Philips.

Philips believes risk management is a value creating activity and as such it is an integral element of the Philips Business System (PBS). Risk management and control supports us in taking sound risk-reward strategic decisions to maximize value creation, it supports sustainable results on our Path to Value, it protects our key strengths (Capabilities, Assets, and Positions) and it supports process excellence.

Philips' risk management focuses on the following risk categories: Strategic, Operational, Compliance and Financial risks. The main risks within these categories are further described in [section 6.2, Risk categories and factors](#), of this Annual Report. The overview highlights the material risks known to Philips, which could hinder it in achieving its strategic and financial business objectives. The risk overview may, however, not include all the risks that may ultimately affect Philips. Some risks not yet known to Philips, or currently believed not to be material, could ultimately have a major impact on Philips' businesses, objectives, revenues, income, assets, liquidity or capital resources.

All forward-looking statements made on or after the date of this Annual Report and attributable to Philips are expressly qualified in their entirety by the factors described in the cautionary statement included in [chapter 17, Forward-looking statements and other information](#), of this Annual Report and the overview of risk factors described in [section 6.2, Risk categories and factors](#), of this Annual Report.

Risk Management Framework

Risk management and control forms an integral part of the Philips business planning and performance review cycle. The company's risk and control policy is designed to provide reasonable assurance that objectives are met by integrating risk assessment in the strategic planning process, integrating management control into the daily operations, ensuring compliance with legal requirements and safeguarding the integrity of the

company's financial reporting and its related disclosures. It makes management responsible for identifying the critical business risks and for the implementation of appropriate risk responses. Philips' risk management approach is embedded in the areas of Corporate Governance, elements of the Philips Business System (Strategic Investment Decision Making, Asset Protection, Operational Excellence, Planning & Performance Cycle), Philips Business Control Framework and Philips General Business Principles. Structured risk assessments take place according to the Philips process standard for managing risk.

Risk appetite

Philips' risk management policy addresses risks related to different categories: Strategic, Operational, Compliance and Financial risks. The Executive Committee and management consider risk appetite when taking decisions and seek to manage risks consistently within the risk appetite. Risk boundaries are set in the various parts of our governance framework including (but not limited to) our Strategy, General Business Principles (GBP), Policies, Philips Business System (PBS), Budgets and Authority schedules. Risk appetite is different for the various risk categories:

- Strategic risks and opportunities may affect Philips' strategic ambitions. Strategic risks include economic and political developments and the need to anticipate and respond timely to market circumstances. Philips is prepared to take considerable strategic risks in a responsible way given the necessity to invest in research & development and manage the portfolio of businesses, including acquisitions and divestments, in a highly uncertain global political and economic environment. Philips carefully evaluates if risk taking is justified in light of Strategic Fit, Portfolio Balance, and overall Value creation ambitions. Philips seeks to avoid risks which dilute or contradict our Brand promise.
- Operational risks include adverse developments resulting from internal processes, people and systems, or from external events that are linked to the actual running of each business (examples are solution and product creation and supply chain management). Our focus on Quality, Excellence and Productivity enhancement guide the day-to-day running and the continuous improvement of our business. Philips takes a calculated approach aimed to optimize the upside and minimize the downside of risks due to the need for high quality of its products and services, reliable and secure IT systems and sustainability commitments.

- Compliance risks cover unanticipated failures to implement, or comply with, appropriate laws, regulations, policies and procedures. Philips attaches prime importance to product quality and safety, including full compliance with regulations and quality standards applicable to our products and services. Being a responsible company everyone in Philips is expected to always act with integrity. Philips rigorously enforces compliance of General Business Principles throughout the Company. Philips has a zero tolerance policy towards non-compliance in relation to breaches of its General Business Principles.
- Financial risks include risks related to Treasury, Accounting and Reporting, Pensions and Tax. Philips is prudent with regard to financial risks as the financial sustainability of the company and investor commitment depends on it. Philips is averse to risks which jeopardize a sustained "Investment grade" credit rating and risks which impede the reliability of our financial reporting. Risk appetite is described further in various chapters of this annual report, including [note 29, Details of treasury / other financial risks](#).

Philips does not classify these risk categories in order of importance.

Corporate Governance

Corporate governance is the system by which a company is directed and controlled. Philips believes that good corporate governance is a critical factor in achieving business success. Good corporate governance derives from, among other things, effective internal controls and high ethical standards. The quality of Philips' system of risk management, business control and other findings of internal and external audits are reported to and discussed by the Audit Committee of the Supervisory Board. Internal auditors monitor the quality of risk management and business controls through the execution of the risk based audit plan as approved by the Audit Committee of the Supervisory Board.

Audit & Risk committees at Group level, Business Groups, Markets and key Functional areas meet quarterly, chaired by first line leadership, to address weaknesses in risk management and business controls structure as reported by internal and external auditors or revealed by self-assessment of management and to take corrective action where necessary. In addition to the Audit Committee, the Quality and Regulatory (Q&R) Committee of the Supervisory Board assists the Supervisory Board in fulfilling its oversight responsibilities particularly in respect of the quality of the Company's products, systems, services and software and the development, testing, manufacturing, marketing and servicing thereof, and regulatory requirements relating thereto. As such, the Q&R Committee supports the Company's risk management in the relevant risk areas. An in-depth description of

Philips' corporate governance structure can be found in [chapter 10, Corporate governance](#), of this Annual Report.

Risk Management

Taking risks is an inherent part of entrepreneurial behavior and well-structured risk management allows management to take risks in a controlled manner. In order to provide a comprehensive view of Philips' risks, structured risk assessments take place according to the Philips process standard for risk management, combining elements of a top-down and bottom-up approach. The process is supported by workshops with management at Business, Market and Group Function levels. During 2017, several risk management workshops were held.



Key elements of the Philips risk management policy are:

- Annual risk assessment for the Group, Business Groups, Markets and key Functions as part of the annual update of the strategic plan. Risks are assessed and prioritized on their impact on objectives, likelihood of occurrence and effectiveness of controls. Management is accountable for the timely development of effective risk responses.

- Developments in the risk profile and management's initiatives to improve risk responses are explicitly discussed and monitored during the quarterly Audit & Risk Committees and in the Quarterly Performance Reviews (QPR).
- As an integral part of the strategy review, the Executive Committee annually assesses the enterprise risk profile, including appropriate risk scenarios and sensitivity analysis, and reviews the potential impact of the enterprise risk profile versus the Group's risk appetite. This risk assessment is based on the latest annual risk assessments of the Group, Business Groups, Markets and key Functions and changes to these, if any, as reported during the periodic review meetings, findings from Philips Internal Audit, Legal and Insurance, the Materiality analysis as described in [chapter 13, Sustainability statements](#), of this Annual Report, views from key stakeholders, external analysis, and risks reported in the annual certification statement on Risk Management and Business Controls.
- Developments in the Enterprise Risk profile and management's initiatives to improve risk responses are discussed and monitored during the quarterly Group Audit & Risk Committee.
- The Executive Committee reviews at least annually the Philips risk management approach and improves the process as required.
- The Philips risk profile and the risk management approach are discussed at least annually with the Audit Committee and with the full Supervisory Board.

Examples of measures taken during 2017 to further strengthen risk management, which have been discussed with the Audit Committee and the full Supervisory Board:

- Execution of the Enterprise Risk Management (ERM) improvement roadmap;
- The continued development of the Information Security Program in light of the increasing exposure to cybercrime and information security requirements resulting from digitalization and a focus on the Healthcare industry;
- The further development of risk management related to long-term service-based business models;
- Introduction of improved comprehensive insurance program;
- Accelerated acquisition integration supported by playbooks;
- Revised plan for GBP deployment for the next 3 years;
- Strengthened Q&R framework and oversight, standardization of Philips Quality Management System across the Company, and Quality improvement campaign;
- Closing of sale of 80.1% interest in Lumileds and sale of substantial part of Lighting resulting in deconsolidation of Philips Lighting during 2017;
- Further de-risking of pension liabilities liabilities with deficit funding in the US defined-benefit plan and settlement of the Brazilian pension plans;

- Continuous improvement of risk dialogues and continuation of risk workshops to cover Business Groups, Markets and Functions.

Philips Business Control Framework

The Philips Business Control Framework (BCF) sets the standard for risk management and business control in Philips. The objectives of the BCF are to maintain integrated management control of the company's operations, in order to ensure the integrity of the financial reporting, as well as compliance with laws and regulations. Philips has designed its BCF based on the "Internal Control-Integrated Framework (2013)" established by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Philips continuously evaluates and improves its BCF to align with business dynamics and good practice.

As part of the BCF, Philips has implemented a global standard for internal control over financial reporting (ICS). ICS, together with Philips' established accounting procedures, is designed to provide reasonable assurance that assets are safeguarded, that the books and records properly reflect transactions necessary to permit preparation of financial statements, that policies and procedures are carried out by qualified personnel and that published financial statements are properly prepared and do not contain any material misstatements. ICS has been deployed in all material reporting units, where business process owners perform an extensive number of controls, document the results each quarter, and take corrective action where necessary. ICS supports business and functional management in a quarterly cycle of assessment and monitoring of its control environment. The findings of management's evaluation are reported to the Executive Committee and the Audit Committee of the Supervisory Board quarterly.

As part of the Annual Report process, management's accountability for business controls is enforced through the formal certification statement sign off by Business Group, Market and Functional management to the Executive Committee. Any deficiencies noted in the design and operating effectiveness of controls over financial reporting which were not completely remediated are evaluated at year-end by the Board of Management. The Board of Management's report, including its conclusions regarding the effectiveness of internal control over financial reporting, can be found in [section 11.1, Management's report on internal control](#), of this Annual Report.

Philips General Business Principles

The Philips General Business Principles (GBP) incorporate and represent the fundamental principles by which all Philips businesses and employees around the globe must abide. They set the minimum standard for business conduct, both for individual employees and for the company and our subsidiaries. Our GBP also serve as a reference for the business conduct we expect from our business partners and suppliers. Translations

of the GBP text are available in 32 languages, allowing almost every employee to read the GBP in their native language. Detailed underlying policies, manuals, training, and tools are in place to give employees practical guidance on how to apply and uphold the GBP in their daily work environments.

The GBP form an integral part of labor contracts in virtually every country in which Philips operates. It is the responsibility of each employee to live up to our GBP, and employees are requested to affirm their commitment to the principles after completing their GBP e-training. In addition, there are separate Codes of Ethics that apply to employees working in specific areas of our business, i.e. the Procurement Code of Ethics and the Financial Code of Ethics. Details can be found at: www.philips.com/gbp. Executives are requested to sign off on the GBP each year to renew their awareness of and reaffirm their compliance with these principles.

Within Philips, the GBP Review Committee is ultimately responsible for the effective deployment of the GBP and for generally promoting a culture of compliance and ethics within the company. The GBP Review Committee is chaired by the Chief Legal Officer, and its members include the Chief HR Officer, the Chief of International Markets and the Chief Financial Officer. They are supported in the implementation of their initiatives by a Committee Secretariat as well as a network of GBP Compliance Officers, who are appointed in all markets, countries and at all major sites where Philips has operations. Furthermore, building on the best practices we have developed in some of our markets, in 2018 all markets will install a formal compliance committee, consisting of (at least) the market leader, the market head of legal and the market CFO, which will deal with GBP related matters on a more granular level.

As part of our unyielding effort to raise GBP awareness and foster dialog throughout the organization, each year a global GBP communications and training plan is deployed. In 2017, a number of initiatives were undertaken through various channels such as new Quick Reference Cards for at-a-glance guidance on how to handle a number of common GBP issues, as well as recurring programs such as e-learning for selected high-risk audiences. For our GBP e-learning, we achieved a training completion rate of 96%. Many of these initiatives contributed to building momentum toward our now annual GBP Dialogue Initiative. In 2017, in order to accommodate the increased demand from the markets and business, we held our Dialogue Initiative over the course of two months beginning in May and ending in June, allowing ample time and scope for teams and leaders alike to arrange and prepare for their dialog session. During the 2017 Dialogue Initiative, more teams at Philips than ever before held open and frank discussions on what Acting with Integrity means to them, and posted pictures of their sessions on the Philips social platform using the hashtag #integritymatters.

The effect of our communication and awareness campaigns is apparent from the results of our biennial Business Integrity Survey. Via this survey, in which tens of thousands of Philips employees participated, we measure employee's perception of integrity throughout the company. For the second time running our scores improved for all the soft-controls we measure.

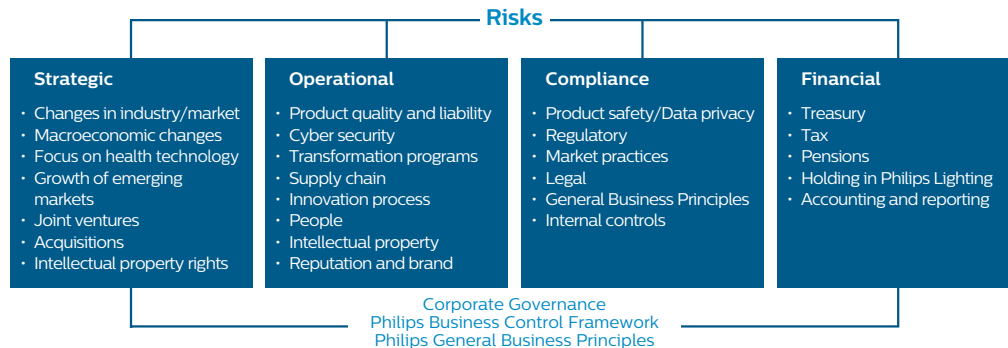
As one of our important controls for monitoring and oversight of the level of GBP compliance within Philips, we deploy quarterly the mandatory GBP self-assessment as part of our Internal Control framework. The GBP Review Committee Secretariat receives an overview of the results of this self-assessment and can take action when deemed necessary. We believe this has created a more robust network to ensure compliance throughout the organization and it has equipped us with the requisite skills and support to monitor and enhance compliance in the increasingly regulated environments in which Philips operates. Furthermore, 2017 saw the creation of a dedicated compliance monitoring team, which will leverage data analytics to quickly identify and address potential compliance issues.

The GBP are supported by established mechanisms that ensure standardized reporting and escalation of concerns where necessary. These mechanisms are based on the GBP Reporting Policy, which urges employees to report any concerns they may have regarding business conduct in relation to the GBP. They can do this either through a GBP Compliance Officer or through the Philips Ethics Line, which enables employees and also third parties to report a concern either by telephone or online in a variety of different languages 24/7 all year round. Concerns raised are registered consistently in a single database hosted outside of Philips servers to ensure confidentiality and security of identity and information. Encouraging people to submit a complaint when they have exhausted all other means of recourse had been – and will continue to be – a cornerstone of our GBP communications and awareness campaign year on year.

Financial Code of Ethics

The Company has a Financial Code of Ethics which applies to the CEO (the principal executive officer) and CFO (the principal financial and principal accounting officer), and to the senior management in the Philips Finance Leadership Team who head the Finance departments of the Company. The Company has published its Financial Code of Ethics within the investor section of its website located at www.philips.com. No changes were considered necessary and no changes have been made to the Financial Code of Ethics since its adoption and no waivers have been granted therefrom to the officers mentioned above in 2017.

For more information, please refer to [sub-section 3.2.8, General Business Principles](#), of this Annual Report.



6.2 Risk categories and factors

In order to provide a comprehensive view of Philips' enterprise risks, structured risk assessments take place in accordance with the Philips process standard to manage risk as described in [section 6.1, Our approach to risk management](#), of this Annual Report. As a result of this process, amongst others, the following actions were performed during 2017:

- In order to reduce its exposure to market risk, Philips continued in 2017 to sell portions of its ownership of Lighting; by the end of 2017 Philips was no longer able to exercise control over Lighting and as a result Lighting has been deconsolidated. Until the completion of the sale of its entire ownership in Philips Lighting, Philips remains exposed to risks with regard to the value of Philips Lighting.
- In 2017 the sale of 80.1% of Lumileds was completed; Philips remains exposed to risks with regard to the value of the remaining 19.9% stake in Lumileds.
- The challenging global political and economic developments had an impact on our results. We have continued to monitor the impact of economic and political developments on our results.
- Philips has strengthened its (cyber) security governance to increase the ability to detect, respond to and close (cyber) security incidents.
- Philips has continued its significant investments in its Quality Management System across the company. Changes in the company-wide quality leadership have been made and new standards and initiatives have been launched.

Philips describes the risk factors within each risk category in order of Philips' current view of expected significance, to give stakeholders an insight into which risks and opportunities it considers more prominent than others at present. The risk overview highlights the main risks and opportunities known to Philips, which could hinder it in achieving its strategic and financial business objectives. The risk overview may, however, not include all the risks that may ultimately affect Philips. Describing risk factors in their order of expected significance within each risk category does not mean that a lower listed risk factor may not have a material and adverse impact on Philips' business, strategic

objectives, revenues, income, assets, liquidity, capital resources or achievement of Philips' goals.

Furthermore, a risk factor described after other risk factors may ultimately prove to have more significant adverse consequences than those other risk factors. Over time Philips may change its view as to the relative significance of each risk factor.

6.3 Strategic risks

Philips may be unable to adapt swiftly to changes in industry or market circumstances, which could have a material adverse impact on its financial condition and results.

Fundamental shifts in the Healthcare industry, like the transition towards digital, may drastically change the business environment. If Philips is unable to recognize these changes in good time, is late in adjusting its business models, or if circumstances arise such as pricing actions by competitors, then this could have a material adverse effect on Philips' growth ambitions, financial condition and operating result.

As Philips' business is global, its operations are exposed to economic and political developments in countries across the world that could adversely impact its financial condition and results.

Philips' business environment is influenced by political and economic conditions in individual and global markets. Financial markets generally showed a stable, favorable performance during 2017 with market volatility at an all-time low; towards the end of 2017 concerns emerged about potential bubbles in some financial markets. Economic growth in China seems to have stabilized. The European Union started to show clear economic growth in 2017 and so far seems unaffected by the lack of progress in the Brexit process. Political uncertainty remains a driver of potential risks in Europe. The weakened government in Great Britain continues to struggle with the Brexit negotiations. The US economy continued to perform well during 2017, but the initial optimism following the start of the new US administration in 2017 has slacked off. The long awaited US Tax Cuts and Jobs Act was only presented at the end

of 2017 and it is uncertain what the impact of this tax reform will be. The US dollar lost strength versus the euro and Japanese yen during the second half of 2017; there is considerable uncertainty about the potential impact of the US Tax Cuts and Jobs Act on the strength of the US dollar. Both Brexit and the policies of the US administration may have significant impact on international trade tariffs and customs laws. Driven by political conflicts, 2017 showed further increases in the quantity and severity of cyber-attacks; some attacks (e.g. WannaCry) affected many countries and public and private organizations. The favorable macroeconomic outlook for the main geographies could quickly reverse due to political conflicts, the unknown impact of changes in US and Eurozone monetary policy and changes in government policies. Uncertainty remains as to the levels of (public) capital expenditures in general, unemployment levels and consumer and business confidence, which could adversely affect demand for products and services offered by Philips.

The general global political environment remains unfavorable for the business environment due to continued political conflicts and terrorism. Numerous other factors, such as regional political conflicts in the Middle East, Turkey, Korean peninsula and other regions, as well as large-scale (in)voluntary migration and profound social instability could continue to impact macroeconomic factors and the international capital and credit markets. It remains difficult to predict changes in, among others, US foreign policy, healthcare and trade and tax laws, the impact of which cannot be predicted. Uncertainty on the timing and the nature of Brexit may adversely affect economic growth and the business environment in the United Kingdom and the European Union. Economic and political uncertainty may have a material adverse impact on Philips' financial condition or results of operations and can also make it more difficult for Philips to budget and forecast accurately. Political instability may have an adverse impact on financial markets which could have a negative impact on the timing and revenues of the sale of the remaining interests in Lighting and the access of Philips to funding. Philips may encounter difficulty in planning and managing operations due to the lack of adequate infrastructure and unfavorable political factors, including unexpected legal or regulatory changes such as foreign exchange import or export controls, increased healthcare regulation, nationalization of assets or restrictions on the repatriation of returns from foreign investments. Given that growth in emerging market countries is correlated to US, Chinese and European economic growth and that such emerging market countries are increasingly important in Philips' operations, the above-mentioned risks are also expected to grow and could have a material adverse effect on Philips' financial condition and results.

Philips' overall risk profile is changing as a result of the focus on Health Technology.

The risk profile of Philips is expected to concentrate focus on one industry due to the dynamics of our changing products and services portfolio, acquisitions and partnerships resulting from the execution of our Health Technology strategy.

Philips' overall performance in the coming years is expected to depend on the realization of its growth ambitions and results in growth geographies.

Growth geographies are becoming increasingly important in the global market. In addition, Asia is an important production, sourcing and design center for Philips. Philips faces strong competition to attract the best talent in tight labor markets and intense competition from local companies as well as other global players for market share in growth geographies. Philips needs to maintain and grow its position in growth geographies, invest in data driven services, invest in local talent, understand developments in end-user preferences and localize the portfolio in order to stay competitive. If Philips fails to achieve these objectives, then this could have a material adverse effect on growth ambitions, financial condition and operating result.

The growth ambitions and the related financial results of Philips may be adversely affected by economic volatility inherent in growth geographies and the impact of changes in macroeconomic circumstances on growth economies.

Philips may not control joint ventures or associated companies in which it invests, which could limit the ability of Philips to identify and manage risks.

Philips has invested and may invest in joint ventures and associated companies in which Philips will have a non-controlling interest. In these cases, Philips has limited influence over, and limited or no control of, the governance, performance and cost of operations of joint ventures and associated companies. Some of these joint ventures and associated companies may represent significant investments and potentially also use Philips' brand. The joint ventures and associated companies that Philips does not control may make business, financial or investment decisions contrary to Philips' interests or may make decisions different from those that Philips itself may have made. Additionally, Philips partners or members of a joint venture or associated company may not be able to meet their financial or other obligations, which could expose Philips to additional financial or other obligations, as well as having a material adverse effect on the value of its investments in those entities or potentially subject Philips to additional claims. Lumileds is an example of a company in which Philips may continue to have a (residual) investment but does not have control.

Acquisitions could expose Philips to integration risks and challenge management in continuing to reduce the complexity of the company.

Philips' acquisitions may expose Philips in the future to integration risks in areas such as sales and service force integration, logistics, regulatory compliance, information technology and finance. Integration difficulties and complexity may adversely impact the realization of an increased contribution from acquisitions. Philips may incur significant acquisition, administrative and other costs in connection with these transactions, including costs related to the integration of acquired businesses. Acquisitions may divert management attention from other business priorities and risks.

Furthermore, organizational simplification expected to be implemented following an acquisition and the resulting cost savings may be difficult to achieve. Acquisitions may also lead to a substantial increase in long-lived assets, including goodwill. Write-downs of these assets due to business developments may have a material adverse effect on Philips' earnings (see also note 11, Goodwill).

Philips' inability to secure and maintain intellectual property rights for products, whilst maintaining overall competitiveness, could have a material adverse effect on its results.

Philips is dependent on its ability to obtain and maintain licenses and other intellectual property (IP) rights covering its products and its design and manufacturing processes. The IP portfolio is the result of an extensive patenting process that could be influenced by a number of factors, including innovation. The value of the IP portfolio is dependent on the successful promotion and market acceptance of standards developed or co-developed by Philips. This is particularly applicable to Personal Health where third-party licenses are important and a loss or impairment could have a material adverse impact on Philips' financial condition and operating results.

6.4 Operational risks

Failure to comply with quality standards, regulations and associated regulatory actions can trigger warranty and product liability claims against Philips and can lead to financial losses and adversely impact Philips' reputation, market share and brand.

Philips is required to comply with the high standards of quality in the manufacture of its medical devices. Philips hereto is subject to the supervision of various national regulatory authorities. Conditions imposed by such national regulatory authorities could result in product recalls or a temporary ban on products and/or production facilities. In addition quality issues and/or liability claims could affect Philips' reputation and its relationships with key customers (both customers for end products and customers that use Philips' products

in their business processes). As a result, depending on the product and manufacturing site concerned and the severity of the quality and/or regulatory issue, this could lead to financial losses through lost revenue and costs of any required remedial actions, and have further impacts on Philips' reputation, market share and brand. Please refer to section 6.5, Compliance risks, of this Annual Report.

A breach in security of, or a significant disruption in, our information technology systems or violation of data privacy laws could adversely affect our operating results, financial condition, reputation and brand.

Philips relies on information technology to operate and manage its businesses and store confidential data (relating to employees, customers, intellectual property, suppliers and other partners); Philips' products, solutions and services increasingly contain sophisticated information technology and generate confidential data related to customers and patients. Like many other multinational companies, Philips is therefore inherently and increasingly exposed to the risk of cyber attacks. Information systems may be damaged, disrupted (including the provision of services to customers) or shut down due to (cyber) attacks by hackers, computer viruses or other malware. In addition, breaches in security of our systems (or the systems of our customers, suppliers or other business partners) could result in the misappropriation, destruction or unauthorized disclosure of confidential information (including intellectual property) or personal data belonging to us or to our employees, partners, customers or suppliers. Successful cyber-attacks may result in substantial costs and other negative consequences, which may include, but are not limited to, lost revenues, reputational damage, remediation costs, and other liabilities to regulators, customers and partners. Furthermore, enhanced protection measures can involve significant costs.

Philips has strengthened its security governance, thus increasing the ability to detect, respond to, and close incidents. Additionally foundational and risk-based security training has been provided throughout the organization. For Mergers & Acquisitions, specific attention is given to ensure a sufficient level of security maturity before and during the M&A processes, including post-merger integration. However, these efforts may prove to be insufficient or unsuccessful.

Although Philips has experienced cyber-attacks and to date has not incurred any significant damage as a result and did not incur significant monetary cost in taking corrective action, there can be no assurance that in the future Philips will be as successful in avoiding damage from cyber-attacks, which could lead to financial losses. Additionally, the integration of new companies and successful outsourcing of business processes are highly dependent on secure and well controlled IT systems.

Diversity in information technology (IT) could result in ineffective or inefficient business management. IT outsourcing and off-shoring strategies could result in complexities in service delivery and contract management.

Philips continuously seeks to create a more open, standardized and cost-effective IT landscape, including through further outsourcing, off-shoring, commoditization and ongoing reduction in the number of IT systems. These changes create risk with regard to the delivery of IT services, the availability of IT systems and the scope and nature of the functionality offered by IT systems. Philips has strengthened the security clauses in supplier contracts, has increased the compliance reviews for those contracts (internally and externally) and has instigated more reviews on key suppliers with regard to information security. However these measures may prove to be insufficient or unsuccessful.

If Philips is unable to ensure effective supply chain management, e.g. facing an interruption of its supply chain, including the inability of third parties to deliver parts, components and services on time, and if it is subject to rising raw material prices, it may be unable to sustain its competitiveness in its markets.

Philips is continuing the process of creating a leaner supply base with fewer suppliers, while maintaining dual/multiple sourcing strategies where possible. This strategy very much requires close cooperation with suppliers to enhance, among other things, time to market and quality. In addition, Philips is continuing its initiatives to replace internal capabilities with less costly outsourced products and services. These processes may result in increased dependency on external suppliers and providers. Although Philips works closely with its suppliers to avoid supply-related problems, there can be no assurance that it will not encounter supply problems in the future or that it will be able to replace a supplier that is not able to meet its demand sufficiently quickly to avoid disruptions.

Shortages or delays could materially harm its business. Most of Philips' activities are conducted outside of the Netherlands, and international operations bring challenges. For example, Philips depends partly on the production and procurement of products and parts from Asian countries, and this constitutes a risk that production and shipping of products and parts could be interrupted by regional conflicts, a natural disaster or extreme weather events resulting from climate change. A general shortage of materials, components or subcomponents as a result of natural disasters also poses the risk of unforeseeable fluctuations in prices and demand, which could have a material adverse effect on Philips' financial condition and operating results.

Philips purchases raw materials, including so-called rare earth metals, copper, steel, aluminum, noble gases and oil-related products, which exposes it to fluctuations in energy and raw material prices. In recent times, commodities have been subject to volatile markets, and such volatility is expected to continue. If Philips is not able to compensate for increased costs or pass them on to customers, price increases could have a material adverse impact on Philips' results. In contrast, in times of falling commodity prices, Philips may not fully benefit from such price decreases, since Philips attempts to reduce the risk of rising commodity prices by several means, including long-term contracting or physical and financial hedging.

Failure to drive operational excellence and productivity in Philips' solution and product creation process and/or increased speed in innovation-to-market could hamper Philips' profitable growth ambitions.

Further improvements in Philips' solution and product creation process, ensuring timely delivery of new solutions and products at lower cost and improvement in customer service levels to create sustainable competitive advantages, are important in realizing Philips' profitable growth ambitions. The emergence of new low-cost competitors, particularly in Asia, further underlines the importance of improvements in the product creation process. The success of new solution and product creation, however, depends on a number of factors, including timely and successful completion of development efforts, market acceptance, Philips' ability to manage the risks associated with new products and production ramp-up issues, the ability of Philips to attract and retain employees with the appropriate skills, the availability of products in the right quantities and at appropriate costs to meet anticipated demand and the risk that new products and services may have quality or other defects in the early stages of introduction. Accordingly, Philips cannot determine in advance the ultimate effect that new solutions and product creations will have on its financial condition and operating results. If Philips fails to create and commercialize products or fails to ensure that end-user insights are translated into solution and product creations that improve product mix and consequently contribution, it may lose its market share and competitiveness, which could have a material adverse effect on its financial condition and operating results.

Because Philips is dependent on its personnel for leadership and specialized skills, the loss of its ability to attract and retain such personnel would have an adverse effect on its business.

The attraction and retention of talented employees in sales and marketing, research and development, finance and general management, as well as of highly specialized technical personnel, especially in transferring technologies to low-cost countries, is critical to Philips' success particularly in times of economic recovery. The loss of specialized skills could

also result in business interruptions. There can be no assurance that Philips will be successful in attracting and retaining highly qualified employees and key personnel needed in the future.

Risk of unauthorized use of intellectual property rights.

Philips produces and sells products and services which incorporate technology protected by intellectual property rights. Philips develops and acquires intellectual property rights on a regular basis. Philips is exposed to the risk that a third party may claim to own the intellectual property rights on technology applied in Philips products and services and that in the event that their claims of infringement of these intellectual property rights are successful, they may be entitled to damages and Philips could incur a fine.

Any damage to Philips' reputation could have an adverse effect on its businesses and brand.

Philips is exposed to developments which could affect its reputation. Such developments could be of an environmental or social nature, connected to the behavior of individual employees or suppliers, or could relate to adherence to regulations related to labor, human rights, health and safety, environmental and chemical management. Reputational damage could materially impact Philips' brand value, financial condition and operating results.

6.5 Compliance risks

Philips is exposed to non-compliance with product safety laws, good manufacturing practices and data privacy.

Philips' brand image and reputation would be adversely impacted by non-compliance with various product safety laws, good manufacturing practices and data protection. In light of Philips' digital strategy, data privacy laws are increasingly important. Also, Diagnosis & Treatment and Connected Care & Health Informatics are subject to various (patient) data protection and safety laws. In Diagnosis & Treatment and Connected Care & Health Informatics, privacy and product safety and security issues may arise, especially with respect to remote access or monitoring of patient data or loss of data on our customers' systems. Philips is exposed to the risk that its products, including components or materials procured from suppliers, may prove to be not compliant with safety laws, e.g. chemical safety regulations. Such non-compliance could result in a ban on the sale or use of these products.

Philips operates in a highly regulated product safety and quality environment. Philips' products are subject to regulation (e.g. the new EU Medical Devices Regulation) by various government agencies, including the FDA (US) and comparable foreign agencies (e.g. CFDA China, MHRA UK, ASNM France, BfArM Germany, IGZ Netherlands). Obtaining their approval is costly and time consuming, but a prerequisite for introducing

products in the market. A delay or inability to obtain the necessary regulatory approvals for new products could have a material adverse effect on business. The risk exists that product safety incidents or user concerns could trigger FDA business reviews which, if failed, could lead to business interruption which in turn could adversely affect Philips' financial condition and operating results.

Philips' global presence exposes the company to regional and local regulatory rules, changes to which may affect the realization of business opportunities and investments in the countries in which Philips operates.

Philips has established subsidiaries in over 80 countries. These subsidiaries are exposed to changes in governmental regulations and unfavorable political developments, which may affect the realization of business opportunities or impair Philips' local investments. Philips' increased focus on the healthcare sector increases its exposure to highly regulated markets, where obtaining clearances or approvals for new products is of great importance, and where there is a dependency on the available funding for healthcare systems. In addition, changes in government reimbursement policies may affect spending on healthcare.

Philips is exposed to governmental investigations and legal proceedings with regard to possible anti-competitive market practices.

National and European authorities are focused on possible anti-competitive market practices. Philips' financial position and results could be materially affected by an adverse final outcome of governmental investigations and litigation, as well as any potential related claims. In the past Philips has been subject to such investigations, litigation and related claims. See also note 24, *Contingent assets and liabilities*.

Legal proceedings covering a range of matters are pending in various jurisdictions against Philips and its current and former group companies. Due to the uncertainty inherent in legal proceedings, it is difficult to predict the final outcome.

Philips, including a certain number of its current and former group companies, is involved in legal proceedings relating to such matters as competition issues, commercial transactions, product liability, participations and environmental pollution. Since the ultimate outcome of asserted claims and proceedings, or the impact of any claims that may be asserted in the future, cannot be predicted with certainty, Philips' financial position and results of operations could be affected materially by adverse outcomes.

Please refer to note 24, *Contingent assets and liabilities*, for additional disclosure relating to specific legal proceedings.

Philips is exposed to non-compliance with business conduct rules and regulations.

Philips' attempts to realize its growth ambitions could expose it to the risk of non-compliance with business conduct rules and regulations, such as anti-bribery provisions. This risk is heightened in growth geographies as the legal and regulatory environment is less developed in growth geographies compared to mature geographies. Examples include commission payments to third parties, remuneration payments to agents, distributors, consultants and the like, and the acceptance of gifts, which may be considered in some markets to be normal local business practice.

Defective internal controls would adversely affect our financial reporting and management process.

The reliability of reporting is important in ensuring that management decisions for steering the businesses and managing both top-line and bottom-line growth are based on reliable data. Flaws in internal control systems could adversely affect the financial position and results and hamper expected growth.

Accurate disclosures provide investors and other market professionals with significant information for a better understanding of Philips' businesses. Imperfections or lack of clarity in disclosures could create market uncertainty regarding the reliability of the data presented and could have a negative impact on the Philips share price.

The reliability of revenue and expenditure data is key for steering the business and for managing top-line and bottom-line growth. The long lifecycle of healthcare sales, from order acceptance to accepted installation, together with the complexity of the accounting rules for when revenue can be recognized in the accounts, presents a challenge in terms of ensuring there is consistency of application of the accounting rules throughout Philips' global business.

6.6 Financial risks

Philips is exposed to a variety of treasury risks and other financial risks including liquidity risk, currency risk, interest rate risk, commodity price risk, credit risk, country risk and other insurable risk.

Negative developments impacting the liquidity of global capital markets could affect the ability of Philips to raise or re-finance debt in the capital markets or could lead to significant increases in the cost of such borrowing in the future. If the markets expect a downgrade or downgrades by the rating agencies or if such a downgrade has actually taken place, this could increase the cost of borrowing, reduce our potential investor base and adversely affect our business.

Philips operates in over 100 countries and its earnings and equity are therefore inevitably exposed to fluctuations in exchange rates of foreign currencies

against the euro. Philips' sales are sensitive in particular to movements in the US dollar, Japanese yen and a wide range of other currencies from developed and emerging markets. Philips' sourcing and manufacturing spend is concentrated in the Eurozone, United States and China. Income from operations is particularly sensitive to movements in currencies from countries where the Group has no manufacturing/sourcing activities or only has manufacturing/sourcing activities on a small scale such as Japan, Canada, Australia and Great Britain and in a range of emerging markets such as Russia, Korea, Indonesia, India and Brazil.

The credit risk of financial and non-financial counterparties with outstanding payment obligations creates exposures for Philips, particularly in relation to accounts receivable with customers and liquid assets and fair values of derivatives and insurance receivables contracts with financial counterparties. A default by counterparties in such transactions can have a material adverse effect on Philips' financial condition and operating results.

Philips is exposed to interest rate risk, particularly in relation to its long-term debt position; this risk can take the form of either fair value or cash flow risk. Failure to effectively hedge this risk can impact Philips' financial condition and operating results.

For further analysis, please refer to [note 29, Details of treasury / other financial risks](#).

Philips is exposed to tax risks, which could have a significant adverse financial impact.

Philips is exposed to tax risks, which could result in double taxation, penalties and interest payments. The source of the risks could lie in local tax rules and regulations as well as in the international and EU regulatory frameworks. These include transfer pricing risks on internal cross-border deliveries of goods and services, tax risks related to acquisitions and divestments, tax risks related to permanent establishments, tax risks relating to tax loss, interest and tax credits carried forward and potential changes in tax law that could result in higher tax expenses and payments. The risks may have a significant impact on local financial tax results which in turn could adversely affect Philips' financial condition and operating results.

The value of the deferred tax assets such as tax losses carried forward is subject to availability of sufficient taxable income within the tax loss-carry-forward period, but also availability of sufficient taxable income within the foreseeable future in the case of tax losses carried forward with an indefinite carry-forward period. The ultimate realization of the Company's deferred tax assets, including tax losses and tax credits carried forward, is dependent upon the generation of future taxable income in the countries where the temporary differences, unused tax losses and unused tax credits were incurred and upon periods during which the

deferred tax assets become deductible. Additionally, in certain instances, realization of such deferred tax assets is dependent upon the successful execution of tax planning strategies. Accordingly, there can be no absolute assurance that all deferred tax assets, such as (net) tax losses and credits carried forward, will be realized.

The US Tax Cuts and Jobs Act enacted in December 2017 has both positive and negative consequences for Philips. Philips has significant tax assets and liabilities in the US as it is an important market for Philips with substantial sales, manufacturing sites and material acquisitions during the past few years. The US Tax Cuts and Jobs Act introduced complex new rules, and further clarifications and guidance by the US authorities are anticipated. These could have a significant financial impact for which Philips will continue monitoring and analyzing any updated guidance.

For further details, please refer to the tax risks paragraph in [note 8, Income taxes](#).

[Philips has defined-benefit pension plans and other post-retirement plans in a number of countries. The funded status and the cost of maintaining these plans are influenced by movements in financial market and demographic developments, creating volatility in Philips' financials.](#)

A significant proportion of (former) employees in Europe and North and Latin America is covered by defined-benefit pension plans and other post-retirement plans. The accounting for such plans requires management to make estimates on assumptions such as discount rates, inflation, longevity, expected cost of medical care and expected rates of compensation. Movements (e.g. due to the movements of financial markets) in these assumptions can have a significant impact on the Defined Benefit Obligation and net interest cost. A negative performance of the financial markets could have a material impact on cash funding requirements and net interest cost and also affect the value of certain financial assets and liabilities of the company.

[Philips is exposed to uncertainty on the timing and proceeds of a sale of Philips Lighting](#)

In 2016, Philips separated its Lighting business and on May 27, 2016, Philips Lighting was listed on the Amsterdam Stock Exchange. Since then Philips Lighting operates as a separate listed company. Philips has subsequently sold a substantial part of its ownership in Philips Lighting and deconsolidated Philips Lighting in 2017. Philips' overall objective is to fully divest its ownership of Philips Lighting. The nature or form, timing and the level of proceeds from this divestment process are uncertain. The timing and level of proceeds will depend on general market conditions and investor appetite for companies of this size and nature. Philips no longer has control over Philips Lighting and has

deconsolidated the assets, liabilities and financial results of Philips Lighting. While Philips holds Philips Lighting as an asset held for sale, Philips' earnings will be affected by changes in the fair value of Philips Lighting.

[Philips is exposed to a number of financial reporting risks, i.e. the risk of material misstatements or errors in its financial reporting.](#)

A risk rating is assigned for each risk identified, based on the likelihood of occurrence and the potential impact of the risk on the financial statements and related disclosures. In determining the probability that a risk will result in a misstatement of a more than inconsequential amount or of a material nature, the following factors are considered to be critical: complexity of the associated accounting activity or transaction process, history of accounting and reporting errors, likelihood of significant (contingent) liabilities arising from activities, exposure to losses, existence of a related party transaction, volume of activity and homogeneity of the individual transactions processed, and changes in accounting characteristics in the prior period compared to the period before that.

For important critical reporting risk areas identified within Philips we refer to the "Use of estimates" section in [note 1, Significant accounting policies](#), as the Company assessed that reporting risk is closely related to the use of estimates and application of judgment.