

2 Group performance

“Our strategic focus on health technology and the successful separation of Lighting has delivered two winning companies and a significant improvement in Group performance. Our net income more than doubled to EUR 1.5 billion while our income from operations increased to EUR 1.9 billion from EUR 1.0 billion in the previous year. Improved earnings and tight management of working capital generated EUR 1.9 billion of cash from our operating activities.”

Abhijit Bhattacharya, CFO Royal Philips

2.1 Financial performance

Management summary

The year 2016

- Sales rose to EUR 17.4 billion, a nominal increase of 4%, in our HealthTech portfolio. On a comparable basis¹⁾ sales increased by 5% in our HealthTech portfolio, which combines our Personal Health businesses, Diagnosis & Treatment businesses, Connected Care & Health Informatics businesses, HealthTech Other and Legacy Items. Lighting posted a 5% decline on a nominal basis and a 2% decline on a comparable basis¹⁾. Overall, Group sales increased by 1% on a nominal basis and 3% on a comparable basis¹⁾, to EUR 24.5 billion.
- Our Personal Health businesses' sales increased to EUR 7,099 million, an increase of 5% on a nominal basis. The 7% growth on a comparable basis¹⁾ was driven by double-digit growth in Health & Wellness and mid-single-digit growth in Personal Care, Sleep & Respiratory Care and Domestic Appliances.
- Our Diagnosis & Treatment businesses' sales amounted to EUR 6,686 million, an increase of 3% on a nominal basis. The 4% growth on a comparable basis¹⁾ was driven by double-digit growth in Image-Guided Therapy and low-single-digit growth in Diagnostic Imaging, while Ultrasound was in line with 2015.
- Our Connected Care & Health Informatics businesses' sales rose to EUR 3,158 million, an increase of 5% on a nominal basis. The 4% growth on a comparable basis¹⁾ was driven by mid-single-digit growth in Patient Care & Monitoring Solutions and low-single-digit growth in Healthcare Informatics, Solutions & Services, partly offset by a low-single-digit decline in Population Health Management.
- Lighting's operational performance continued to improve year-on-year. Sales in 2016 were EUR 7,094 million. Comparable sales¹⁾ reflected double-digit growth in LED and Home, which was more than offset by a double-digit decline in Lamps and a low-single-digit decline in Professional.
- In line with our mission to improve people's lives, we have embedded sustainability at the heart of our business processes, and Green Revenues, including products and solutions sales, increased to 64% of total revenues in 2016. In recognition of our sustainability achievements, Philips was named industry group leader in the Capital Goods category in the 2016 Dow Jones Sustainability Index.
- Net income amounted to EUR 1.5 billion and increased by EUR 832 million compared to 2015, driven by improved performance in the HealthTech portfolio and in Lighting as well as the Funai arbitration award, partly offset by higher financial expenses and tax charges. Net income is not allocated to segments as certain income and expense line items are monitored on a centralized basis.
- EBITA¹⁾ totaled EUR 2.2 billion, compared to EUR 1.4 billion a year earlier. Our three cost savings programs all delivered ahead of plan in 2016. We achieved EUR 269 million of gross savings in overhead costs, EUR

418 million of gross savings in procurement, and our End2End process improvement program delivered productivity savings of EUR 204 million.

- Net cash provided by operating activities increased from EUR 1.2 billion in 2015 to EUR 1.9 billion, mainly due to higher earnings and lower outflows related to pension de-risking settlements, partly offset by a EUR 280 million outflow related to the Masimo agreements and a EUR 91 million premium payment related to the October 2016 bond redemption.
- As of October 20, 2016, Philips had completed the 3-year EUR 1.5 billion share buy-back program. During the year Philips returned EUR 868 million in dividends and shares repurchase.

Philips Group
Key data in millions of EUR unless otherwise stated
2014 – 2016

	2014	2015	2016
Condensed statement of income			
Sales	21,391	24,244	24,516
Income from operations (EBIT)	486	992	1,882
as a % of sales	2.3%	4.1%	7.7%
EBITA ¹⁾	821	1,372	2,235
as a % of sales	3.8%	5.7%	9.1%
Financial income and expenses	(301)	(369)	(493)
Income tax expense	(26)	(239)	(327)
Investments in associates	62	30	13
Income from continuing operations	221	414	1,075
Income from Discontinued operations – net of income tax	190	245	416
Net income	411	659	1,491
Other indicators			
Net income attributable to shareholders per common share in EUR:			
basic	0.45	0.70	1.58
diluted	0.45	0.70	1.56
Net cash provided by operating activities	1,303	1,167	1,904
Net capital expenditures	(806)	(842)	(831)
Employees (FTEs)	113,678	112,959	114,731
Continuing operations	105,365	104,204	105,223
Discontinued operations	8,313	8,755	9,508

2.1.1 Sales

The composition of sales growth in percentage terms in 2016, compared to 2015, is presented in the table below.

Philips Group
Sales growth composition in %
2016 versus 2015

	nominal growth	currency effects	consolidation changes	comparable growth ¹⁾
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
HealthTech Other	(5.0)	0.0	0.0	(5.0)
Lighting	(4.6)	2.1	0.2	(2.3)
Philips Group	1.1	1.4	0.2	2.7

Group sales amounted to EUR 24,516 million in 2016, which represents 1% nominal growth compared to 2015. Adjusted for a 2% negative currency effect and consolidation impact, comparable sales¹⁾ were 3% above 2015.

Our Personal Health businesses' sales amounted to EUR 7,099 million, which was EUR 348 million higher than in 2015, or 5% higher on a nominal basis. The 7% growth on a comparable basis¹⁾ was driven by double-digit growth in Health & Wellness, and mid-single-digit growth in Personal Care, Domestic Appliances and Sleep & Respiratory Care. From a geographic perspective, on a comparable basis¹⁾ both mature and growth geographies, achieved high-single-digit growth.

Our Diagnosis & Treatment businesses' sales amounted to EUR 6,686 million, which was EUR 202 million higher than in 2015, or 3% higher on a nominal basis. The 4% growth on a comparable basis¹⁾ was driven by double-digit growth in Image-Guided Therapy, low-single-digit growth in Diagnostic Imaging, while Ultrasound was in line with 2015. From a geographic perspective, comparable sales¹⁾ in growth geographies showed double-digit growth, while mature geographies sales were in line with 2015.

Our Connected Care & Health Informatics businesses' sales amounted to EUR 3,158 million, which was EUR 136 million higher than in 2015, or 5% higher on a nominal basis. The 4% growth on a comparable basis¹⁾ reflected mid-single-digit growth in Patient Care & Monitoring Solutions, low-single-digit growth in Healthcare Informatics, Solutions & Services and a low-single-digit decline in Population Health Management. From a geographic perspective, comparable sales¹⁾ in mature geographies showed mid-single-digit growth, while growth geographies sales reported low-single-digit growth.

Lighting sales amounted to EUR 7,094 million, which was EUR 344 million lower than in 2015 and 5% lower on a nominal basis. The 2% decline on a comparable basis¹⁾ reflected double-digit growth in LED and Home, which was more than offset by an anticipated double-digit decline at Lamps and a low-single-digit decline at

Professional. From a geographic perspective, comparable sales¹⁾ showed a low-single-digit decline in growth and mature geographies.

HealthTech Other reported sales of EUR 478 million, which reflected EUR 38 million lower royalty income due to the foreseen expiration of licenses, partly offset by one-time patent license deals and strong double-digit growth in Emerging Businesses.

2.1.2 Earnings

In 2016, Philips' gross margin was EUR 10,612 million, or 43.3% of sales, compared to EUR 9,856 million, or 40.7% of sales, in 2015. Gross margin in 2016 included EUR 107 million of restructuring and acquisition-related charges, whereas 2015 included EUR 176 million of restructuring and acquisition-related charges. 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. Gross margin in 2015 also included charges of EUR 35 million related to the devaluation of the Argentine peso, a EUR 28 million currency revaluation of the provision for the Masimo litigation and EUR 3 million related to the separation of the Lighting business. The year-on-year increase was driven by improved performance in the HealthTech portfolio and in Lighting, as well as lower restructuring and acquisition-related charges.

Selling expenses increased from EUR 5,815 million in 2015 to EUR 5,888 million in 2016. Selling expenses as a % of total sales remained in line with 2015 at 24.0%. Selling expenses in 2016 included EUR 67 million of restructuring and acquisition-related charges, compared to EUR 62 million of restructuring and acquisition-related charges in 2015. Selling expenses in 2016 included EUR 38 million related to the separation of the Lighting business, while 2015 included charges of EUR 31 million related to a legal provision and EUR 69 million related to the separation of the Lighting business.

Research and development costs increased from EUR 1,927 million, or 7.9% of sales, in 2015 to EUR 2,021 million, or 8.2% of sales, in 2016. Research and development costs in 2016 included EUR 34 million of restructuring and acquisition-related charges, compared to EUR 16 million in 2015. The year-on-year increase was mainly due to higher spend in the Personal Health businesses and Diagnosis & Treatment businesses, as well as higher restructuring and acquisition-related charges.

General and administrative expenses amounted to EUR 845 million, or 3.4% of sales, in 2016, compared to EUR 1,209 million, or 5.0% of sales, in 2015. 2016 included EUR 5 million of restructuring and acquisition-related charges, compared to EUR 30 million in 2015. 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. 2015 also included charges of EUR 345 million mainly related to settlements for pension de-risking and EUR 111 million related to the separation of the Lighting business.

The overview below shows sales, income from operations (EBIT) and EBITA¹⁾ according to the 2016 segment classifications.

Philips Group
Sales, Income from operations (EBIT) and EBITA¹⁾
in millions of EUR unless otherwise stated
2015 – 2016

	Sales	Income from operations (EBIT)	%	EBITA ¹⁾	%
2016					
Personal Health	7,099	953	13.4%	1,092	15.4%
Diagnosis & Treatment	6,686	546	8.2%	594	8.9%
Connected Care & Health Informatics	3,158	275	8.7%	322	10.2%
HealthTech Other	478	(129)		(120)	
Lighting	7,094	432	6.1%	542	7.6%
Legacy Items	1	(195)		(195)	
Philips Group	24,516	1,882	7.7%	2,235	9.1%

2015					
Personal Health	6,751	736	10.9%	885	13.1%
Diagnosis & Treatment	6,484	322	5.0%	377	5.8%
Connected Care & Health Informatics	3,022	173	5.7%	227	7.5%
HealthTech Other	503	49		64	
Lighting	7,438	334	4.5%	441	5.9%
Legacy Items	46	(622)		(622)	
Philips Group	24,244	992	4.1%	1,372	5.7%

¹⁾ Non-GAAP financial measure. For the definition and reconciliation to the most directly comparable GAAP measure, refer to [chapter 4, Reconciliation of non-GAAP information](#), of this Annual Report.

In 2016, income from operations (EBIT) increased by EUR 890 million year-on-year to EUR 1,882 million, or 7.7% of sales. Restructuring and acquisition-related charges amounted to EUR 213 million, compared to EUR 283 million in 2015. Income from operations (EBIT) in 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. Income from operations (EBIT) in 2015 also included charges of EUR 183 million related to the separation of the Lighting business, EUR 345 million mainly related to settlements for pension de-risking, EUR 35 million related to the devaluation of the Argentine peso, EUR 31 million relating to legal provisions, EUR 28 million related to the currency revaluation of the provision for the Masimo litigation, and a EUR 37 million gain related to the sale of real estate assets.

Amortization and impairment of intangibles, excluding software and capitalized product development costs, amounted to EUR 350 million in 2016, compared to EUR

¹⁾ Non-GAAP financial measure. For the definition and reconciliation to the most directly comparable GAAP measure, refer to [chapter 4, Reconciliation of non-GAAP information](#), of this Annual Report.

380 million in 2015. In 2016, goodwill impairment charges amounted to EUR 3 million consisting of impairments on divested businesses in Lighting, see [note 11, Goodwill](#). In 2015 goodwill impairment charges were nil.

EBITA¹⁾ increased from EUR 1,372 million, or 5.7% of sales, in 2015 to EUR 2,235 million, or 9.1% of sales, in 2016. The year-on-year increase was driven by improved performance at all segments except HealthTech Other.

Personal Health businesses

In 2016, income from operations (EBIT) totaled EUR 953 million, compared to EUR 736 million in 2015. EBITA¹⁾ amounted to EUR 1,092 million, or 15.4% of sales, compared to EUR 885 million, or 13.1% of sales, in 2015. EBITA¹⁾ included restructuring and acquisition-related charges of EUR 16 million, compared to EUR 37 million in 2015. EBITA¹⁾ in 2015 also included charges of EUR 31 million relating to legal provisions and charges of EUR 13 million related to the devaluation of the Argentine peso. The year-on-year increase was mainly attributable to higher volumes and cost productivity.

Diagnosis & Treatment businesses

In 2016, income from operations (EBIT) totaled EUR 546 million, compared to EUR 322 million in 2015. EBITA¹⁾ amounted to EUR 594 million, or 8.9% of sales, compared to EUR 377 million, or 5.8% of sales, in 2015. EBITA¹⁾ included restructuring and acquisition-related charges of EUR 37 million, compared to EUR 131 million in 2015. 2015 also included charges of EUR 7 million related to the devaluation of the Argentine peso. The year-on-year increase was largely driven by Image-Guided Therapy and Diagnostic Imaging, as well as lower restructuring and acquisition-related charges.

Connected Care & Health Informatics businesses

In 2016, income from operations (EBIT) totaled EUR 275 million, compared to EUR 173 million in 2015. EBITA¹⁾ amounted to EUR 322 million, or 10.2% of sales, compared to EUR 227 million, or 7.5% of sales, in 2015. EBITA¹⁾ included restructuring and acquisition-related charges of EUR 14 million, compared to EUR 38 million in 2015. 2016 also included a EUR 12 million net release of provisions, while 2015 also included a EUR 28 million charge related to the currency revaluation of the Masimo provisions and charges of EUR 1 million related to the devaluation of the Argentine peso. The increase was mainly driven by higher volumes and lower restructuring and acquisition-related charges and other items, partly offset by higher expenditure on innovation.

HealthTech Other

In 2016, income from operations (EBIT) totaled EUR (129) million, compared to EUR 49 million in 2015. EBITA¹⁾ amounted net cost of EUR 120 million, compared to a gain of EUR 64 million in 2015. EBITA¹⁾ included restructuring and acquisition-related charges

of EUR 28 million and a EUR 26 million impairment of real estate assets, compared to a net restructuring release of EUR 19 million and a EUR 37 million gain related to the sale of real estate assets in 2015. The year-on-year decrease was mainly attributable to higher restructuring and acquisition-related charges and other items, investments in Emerging Businesses, brand campaigns and cyber security.

Lighting

In 2016, income from operations (EBIT) totaled EUR 432 million, compared to EUR 334 million in 2015. EBITA¹⁾ amounted to EUR 542 million, or 7.6% of sales, a year-on-year increase of EUR 101 million. Restructuring and acquisition-related charges in 2016 amounted to EUR 119 million, compared to EUR 97 million in 2015. EBITA¹⁾ in 2016 also included a gain of EUR 14 million related to a release of provisions originating from the separation activities, compared to EUR 14 million of charges related to the devaluation of the Argentine peso in 2015. The increase was mainly attributable to cost reduction programs and an increase in gross margin, partly offset by higher restructuring and acquisition-related charges.

Legacy Items

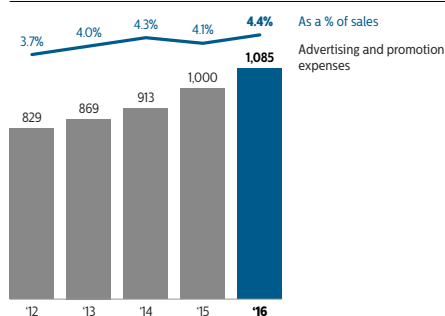
Income from operations (EBIT) mainly included EUR 152 million of charges related to the separation of the Lighting business, a EUR 14 million charge related to provisions originating from the separation of the Lighting business, EUR 9 million of costs of addressing legacy issues related to environmental provisions, EUR 4 million of pension costs, EUR 36 million of stranded costs related to the combined Lumileds and Automotive businesses, EUR 11 million of charges related to various provisions, as well as a EUR 46 million gain from the settlement of a pension-related claim. Income from operations (EBIT) in 2015 included EUR 345 million of settlements mainly related to pension de-risking.

2.1.3 Advertising and promotion

Philips' total advertising and promotion expenses were EUR 1,085 million in 2016, an increase of 9% compared to 2015. The increase was mainly due to investments in key mature geographies such as the United States and Japan, as well as Germany. The total advertising and promotion investment as a percentage of sales was 4.4% in 2016, compared to 4.1% in 2015.

Philips' brand value increased by 4% to over USD 11.3 billion as measured by Interbrand. In the 2016 listing, Philips is ranked the 41st most valuable brand in the world.

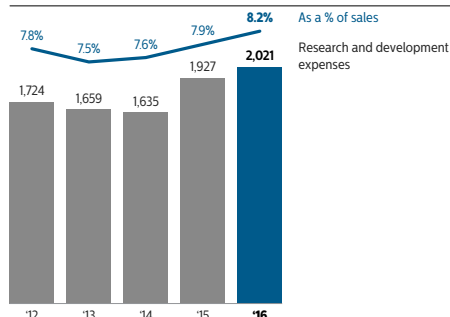
Philips Group
Advertising and promotion expenses in millions of EUR
2012 – 2016



2.1.4 Research and development

Research and development costs increased from EUR 1,927 million in 2015 to EUR 2,021 million in 2016. Research and development costs in 2016 included EUR 35 million of restructuring and acquisition-related charges, compared to EUR 16 million in 2015. The year-on-year increase was mainly due to higher spend at the Personal Health businesses and the Diagnosis & Treatment businesses. As a percentage of sales, research and development costs increased from 7.9% in 2015 to 8.2% in 2016.

Philips Group
Research and development expenses in millions of EUR
2012 – 2016



Philips Group
Research and development expenses in millions of EUR
2014 – 2016

	2014	2015	2016
Personal Health	332	383	412
Diagnosis & Treatment	455	596	629
Connected Care & Health Informatics	289	386	388
HealthTech Other	153	189	219
Lighting	395	365	350
Legacy Items	11	8	23
Philips Group	1,635	1,927	2,021

2.1.5 Pensions

In 2016, the total costs of post-employment benefits amounted to EUR 53 million for defined-benefit plans and EUR 382 million for defined-contribution plans, compared to EUR 559 million and EUR 293 million respectively in 2015.

The above 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 66 million in 2016 (2015: EUR 72 million).

2016 included a legal claim settlement gain of EUR 46 million related to the UK pension plan, a EUR 8 million settlement gain related to de-risking actions in the US and a combined settlement loss of EUR 2 million in other countries. Past-service cost gains of EUR 8 million were recognized in 2016 relating to a number of small plan changes.

2015 included settlement costs of EUR 329 million mainly related to the settlement of the UK plan, results of other de-risking actions in the UK prior to the settlement and the settlement of parts of the US pension plan. Past-service costs of EUR 14 million were recognized related to de-risking actions taken in the UK prior to the settlement of the plan, including a past-service cost for GMP Equalization in the same UK plan. Some smaller plan changes in other countries resulted in a small past-service cost gain.

In 2015, the total costs of post-employment benefits amounted to EUR 559 million for defined-benefit plans and EUR 293 million for defined-contribution plans, compared to EUR 241 million and EUR 144 million respectively in 2014.

The overall funded status 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. The pension deficit recognized in the balance sheet decreased for the same reasons.

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

2.1.6 Restructuring and impairment charges

In 2016, income from operations (EBIT) included net charges totaling EUR 173 million for restructuring. 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 3 million.

In 2015, income from operations (EBIT) included net charges totaling EUR 171 million for restructuring and the goodwill impairment was nil.

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

In 2016, the most significant restructuring projects were mainly related to Lighting and HealthTech Other. Restructuring projects at HealthTech Other were mainly to overhead cost reduction programs and took place in the Netherlands. Restructuring projects at Lighting were related to manufacturing footprint rationalization and simplification of the business structure, and mainly took place in France and Belgium.

In 2015, the most significant restructuring projects were related to Lighting, Diagnosis & Treatment businesses and Connected Care & Health Informatics businesses.

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

Philips Group
Restructuring and related charges in millions of EUR
2014 – 2016

	2014	2015	2016
Restructuring and related charges per segment:			
Personal Health	16	38	16
Diagnosis & Treatment	47	25	6
Connected Care & Health Informatics	31	37	9
HealthTech Other	58	(20)	27
Lighting	262	90	115
Legacy Items	-	1	-
Continuing operations	414	171	173
Discontinued operations	18	5	5
Cost breakdown of restructuring and related charges:			
Personnel lay-off costs	354	194	158
Release of provision	(36)	(88)	(61)
Restructuring-related asset impairment	57	46	38
Other restructuring-related costs	39	19	38
Continuing operations	414	171	173
Discontinued operations	18	5	5

2.1.7 Financial income and expenses

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

Philips Group
Financial income and expenses in millions of EUR
2014 – 2016

	2014	2015	2016
Interest expense (net)	(251)	(302)	(327)
Sale of securities	60	20	3
Impairments	(17)	(46)	(27)
Other	(93)	(41)	(142)
Financial income and expenses	(301)	(369)	(493)

Net interest expense in 2016 was EUR 25 million higher than in 2015, mainly driven by higher interest expense resulting from higher average debt.

Impairments amounted to EUR 27 million, mainly due to Corindus Vascular Robotics.

Other financial expense amounted to EUR 142 million in 2016, primarily consisting of financial charges related to the early redemption of USD bonds in October 2016 and January 2017.

For further information, refer to [note 7, Financial income and expenses](#).

2.1.8 Income taxes

Income taxes amounted to EUR 327 million, compared to EUR 239 million in 2015. The effective income tax rate in 2016 was 23.5%, compared to 38.4% in 2015. The decrease was largely due to a change in the geographical mix of actual profits and one-off tax benefits in 2016 mainly relating to recognition of deferred tax assets.

For 2017, we expect our effective tax rate to be around 30%. However, the actual rate will depend on the geographical mix of profits.

For further information, refer to [note 8, Income taxes](#).

2.1.9 Results of investments in associates

Results related to investments in associates decreased from a gain of EUR 30 million in 2015 to a gain of EUR 13 million in 2016, mainly reflecting the proceeds from the sale of Assembléon Technologies B.V. in 2015.

For further information, refer to [note 5, Interests in entities](#).

2.1.10 Non-controlling interests

Net income attributable to non-controlling interests increased from EUR 14 million in 2015 to EUR 43 million in 2016, mainly as a result of the sale of the 28.775% minority interest in Philips Lighting.

2.1.11 Discontinued operations

Discontinued operations consist primarily of the combined businesses of Lumileds and Automotive, the Audio, Video, Multimedia & Accessories business, 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 2014, Philips announced the start of the process to combine the Lumileds and Automotive Lighting businesses into a stand-alone company and explore strategic options to attract capital from third-party investors for this combined business.

In January 2016, Philips announced that the transaction with Go Scale Capital had been terminated despite efforts to mitigate the concerns of the Committee on Foreign Investment in the United States ('CFIUS').

Philips announced December 12, 2016 that it has signed an agreement to sell an 80.1% interest in Lumileds, a leading supplier of LED components and automotive

lighting, to certain funds managed by affiliates of Apollo Global Management, LLC (NYSE: APO). Philips will retain the remaining 19.9% interest in Lumileds.

Philips Group
Net income of Discontinued operations
 in millions of EUR unless otherwise stated
 2014 – 2016

	2014	2015	2016
The combined Lumileds and Automotive businesses	141	246	282
Other	49	(1)	134
Net income of Discontinued operations	190	245	416

In 2016, income from Discontinued operations increased by EUR 171 million to EUR 416 million. The year-on-year increase was mainly due to improved results of the combined Lumileds and Automotive businesses, which were driven by higher sales and improvements in Gross margin, and the Funai arbitration award of EUR 144 million, which includes disbursements and interest as compensation for damages.

In 2015, income from Discontinued operations increased by EUR 55 million to EUR 245 million. The year-on-year increase was mainly due to the positive impact from the treatment of depreciation and amortization of assets held for sale of the combined Lumileds and Automotive businesses.

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

2.1.12 Net income

Net income increased from EUR 659 million in 2015 to EUR 1,491 million in 2016. The increase was largely due to higher income from operations (EBIT) of EUR 890 million and net income from Discontinued operations of EUR 171 million, partly offset by higher financial charges of EUR 124 million, higher income tax charges of EUR 88 million and EUR 17 million lower net income from investments in associates.

Basic earnings per common share from net income attributable to shareholders increased from EUR 0.70 per common share in 2015 to EUR 1.58 per common share in 2016.

2.1.13 Acquisitions and divestments

Acquisitions

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 post-merger integration charges of EUR 31 million in the Diagnosis & Treatment businesses, EUR 4 million in the Connected Care & Health Informatics businesses and EUR 3 million in Lighting.

In 2015, Philips completed four acquisitions, the largest being Volcano Corporation, an image-guided therapy company based in the United States, and Blue Jay Consulting, a leading provider of hospital emergency room consulting services. Acquisitions in 2015 and prior years led to post-merger integration charges of EUR 107 million, mainly in the Diagnosis & Treatment businesses, and EUR 5 million in Lighting.

In 2014, Philips acquired Unisensor, a Danish healthcare company, and a 51% interest in General Lighting Company (GLC) based in the Kingdom of Saudi Arabia. Philips also purchased some minor magnetic resonance imaging (MRI) activities from Hologic, a US healthcare company. Acquisitions in 2014 and prior years led to post-merger integration charges of EUR 1 million in the Diagnosis & Treatment businesses, EUR 1 million in the Personal Health businesses and EUR 19 million in Lighting.

Divestments

In 2016, Philips completed six divestments, mainly several small businesses within Lighting.

In 2015, Philips completed seven divestments, which included, the sale of Assembléon Holding B.V., OEM Remote Controls, Axsun Technologies LLC, and several small businesses within the HealthTech portfolio and Lighting.

In 2014, Philips completed the divestment of its Lifestyle Entertainment activities to Gibson Brands Inc. Philips also completed two other divestments of business activities which related to the HealthTech portfolio and Lighting activities.

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

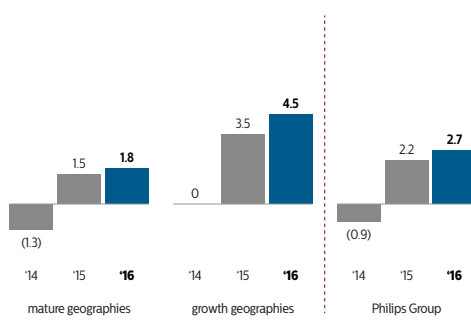
2.1.14 Performance by geographic cluster

In 2016, sales increased 1% nominally, largely due to unfavorable foreign exchange impacts, and 3% on a comparable basis¹⁾, driven by 5% comparable sales growth¹⁾ in the HealthTech portfolio.

Sales in mature geographies were EUR 312 million higher than in 2015, or 2% higher on both a nominal and comparable basis¹⁾. Sales in Western Europe were 2% higher than in 2015, with growth in the Diagnosis & Treatment businesses and Personal Health businesses, partly offset by a decline in the Connected Care & Health Informatics businesses and Lighting. Sales in North America increased by EUR 166 million, or 2% on a comparable basis¹⁾. Comparable sales¹⁾ in other mature geographies showed a 2% increase, with growth in the Connected Care & Health Informatics businesses and Personal Health businesses, while Diagnosis & Treatment businesses declined 1% and Lighting was in line with 2015.

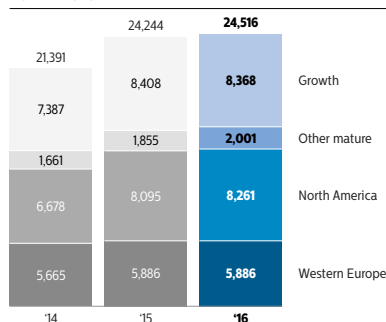
In growth geographies, sales were flat year-on-year on a nominal basis. The 5% increase on a comparable basis⁹⁾ reflected double-digit growth in the Diagnosis & Treatment businesses, high-single-digit growth in the Personal Health businesses and low-single-digit growth in the Connected Care & Health Informatics businesses, partly offset by a low-single digit decline at Lighting. The increase was driven by double-digit growth in Central & Eastern Europe, high-single-digit growth in Latin America and mid-single-digit growth in China, partly offset by a mid-single-digit decline in Middle East & Turkey.

Philips Group
Comparable sales growth by geographic cluster⁹⁾ in %
2014 – 2016



⁹⁾ Non-GAAP financial measure. For the definition and reconciliation to the most directly comparable GAAP measure, refer to chapter 4, Reconciliation of non-GAAP information, of this Annual Report.

Philips Group
Sales by geographic cluster in millions of EUR
2014 – 2016

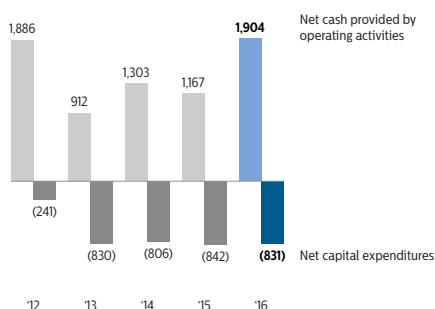


2.1.15 Net cash provided by (used for) continuing operations

Net cash provided by operating activities

Net cash provided by operating activities amounted to EUR 1,904 million in 2016, which was EUR 737 million higher than in 2015, mainly due to higher earnings, net improvements in accounts payable, accrued liabilities and other current liabilities, receivables and other current assets and inventories related inflows and the higher outflows recorded in 2015 related to CRT litigation claims and pension de-risking settlements.

Philips Group
Net cash provided by operating activities and net capital expenditures in millions of EUR
2012 – 2016



Condensed consolidated statements of cash flows for the years ended December 31, 2014, 2015 and 2016 are presented below:

Philips Group
Condensed consolidated cash flow statements⁹⁾
in millions of EUR
2014 – 2016

	2014	2015	2016
Net cash provided by operating activities	1,303	1,167	1,904
Net cash used for investing activities	(984)	(1,941)	(1,167)
Net capital expenditures	(806)	(842)	(831)
Other investing cash flows	(178)	(1,099)	(336)
Net cash provided by (used for) financing activities	(1,189)	508	(420)
Net cash provided by (used for) continuing operations	(870)	(266)	317
Net cash provided by (used for) Discontinued operations	193	79	268
Effect of changes in exchange rates on cash and cash equivalents	85	80	(17)
Total change in cash and cash equivalents	(592)	(107)	568
Cash and cash equivalents at the beginning of year	2,465	1,873	1,766
Cash and cash equivalents at the end of year	1,873	1,766	2,334

⁹⁾ Please refer to section 10.7, Consolidated statements of cash flows, of this Annual Report

Net cash used for investing activities

Other investing cash flows

In 2016, acquisitions of businesses (including acquisition of investments in associates) amounted to a cash outflow of EUR 202 million.

Net cash proceeds from divestment of businesses amounted to EUR 31 million and were received mainly from divested businesses held for sale.

Net cash outflow from non-current financial assets of EUR 45 million was mainly due to the acquisition of stakes in investment funds.

EUR 120 million net cash used for derivatives and current financial assets was mainly due to EUR 132 million cash paid with respect to foreign exchange derivative contracts related to activities for liquidity management funding.

In 2015, acquisitions of businesses (including acquisition of investments in associates) amounted to a cash outflow of EUR 1,116 million which was mainly related to the acquisition of Volcano.

Net cash proceeds from divestment of businesses amounted to EUR 57 million and were received mainly from the divestment of Assembleon Holding B.V., the OEM remote control business and Axsun Technologies LLC.

Net cash inflow from non-current financial assets of EUR 32 million was mainly due to the sale of stakes in Silicon & Software Systems and other equity interest.

EUR 72 million net cash used for derivatives and current financial assets was mainly due to EUR 193 million cash paid with respect to foreign exchange derivative contracts related to activities for liquidity management funding, partially offset by EUR 121 million received with respect to current financial assets mainly related to TPV Technology Limited loans.

Net cash (used for) provided by financing activities

Net cash used for financing activities in 2016 was EUR 420 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. The net impact of changes in debt was a decrease of EUR 377 million. Additionally, net cash outflows for share buy-back and share delivery totaled EUR 526 million.

Net cash provided by financing activities in 2015 was EUR 508 million. Philips' shareholders were given EUR 730 million in the form of a dividend, of which the cash portion of the dividend amounted to EUR 298 million. The net impact of changes in debt was an increase of EUR 1,231 million. Additionally, net cash outflows for share buy-back and share delivery totaled EUR 425 million.

2.1.16 Cash flows from discontinued operations

In 2016, cash inflow from Discontinued operations as reported within operating activities amounted to EUR 268 million, mainly attributable to a cash inflow of EUR 148 million from the Automotive and Lumileds businesses and a cash inflow from the Audio, Video, Multimedia & Accessories business of EUR 119 million.

In 2015, cash inflow from Discontinued operations as reported within operating activities amounted to EUR 79 million, mainly attributable to a cash inflow of EUR 115 million from the Automotive and Lumileds

businesses, offset by a cash outflow from the Audio, Video, Multimedia & Accessories business of EUR 37 million.

2.1.17 Financing

Condensed consolidated balance sheets for the years 2014, 2015 and 2016 are presented below:

Philips Group
Condensed consolidated balance sheet¹⁾ in millions of EUR
2014 – 2016

	2014	2015	2016
Intangible assets	10,526	12,216	12,450
Property, plant and equipment	2,095	2,322	2,155
Inventories	3,314	3,463	3,392
Receivables	5,040	5,287	5,636
Assets held for sale	1,613	1,809	2,180
Other assets	3,891	4,113	4,156
Payables	(5,282)	(5,604)	(6,028)
Provisions ³⁾	(4,517)	(4,243)	(3,606)
Liabilities directly associated with assets held for sale	(349)	(407)	(525)
Other liabilities ¹⁾	(3,132)	(3,182)	(3,030)
Net asset employed	13,199	15,774	16,780
Cash and cash equivalents	1,873	1,766	2,334
Debt	(4,104)	(5,760)	(5,606)
Net debt²⁾	(2,231)	(3,994)	(3,272)
Non-controlling interests	(101)	(118)	(907)
Shareholders' equity	(10,867)	(11,662)	(12,601)
Financing	(13,199)	(15,774)	(16,780)

¹⁾ Please refer to section 10.6, Consolidated balance sheets, of this Annual Report

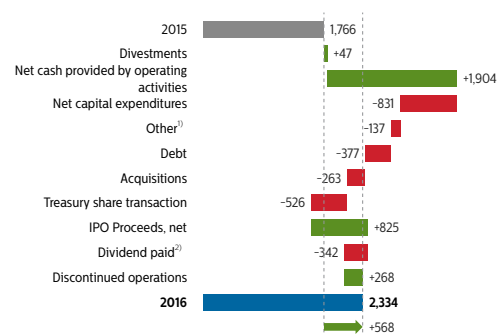
²⁾ Non-GAAP financial measure. For the definition and reconciliation to the most directly comparable GAAP measure, refer to chapter 4, Reconciliation of non-GAAP information, of this Annual Report.

³⁾ Adjusted to reflect a reclassification of net defined-benefit obligations into Long-term provisions. See note 1, Significant accounting policies

2.1.18 Cash and cash equivalents

In 2016, cash and cash equivalents increased by EUR 568 million to EUR 2,334 million at year-end. The increase was mainly attributable to cash inflows of EUR 1,904 million from net cash provided by operating activities, EUR 825 million net proceeds from Philips Lighting IPO and EUR 268 million from Discontinued operations. This was partly offset by cash outflows of EUR 831 million from net capital expenditures, EUR 526 million from treasury share transactions, EUR 377 million from decreases in debt, cash dividends paid of EUR 342 million including EUR 12 million of dividends paid to non-controlling interest and EUR 263 million related to acquisitions.

Philips Group
Cash balance movements in millions of EUR
 2016



¹⁾ Includes cash flow for derivatives and currency effect

²⁾ Includes dividends paid to shareholders of Koninklijke Philips N.V. and to non-controlling interests

2.1.19 Debt position

Total debt outstanding at the end of 2016 was EUR 5,606 million, compared with EUR 5,760 million at the end of 2015.

Philips Group
Changes in debt in millions of EUR
 2014 – 2016

	2014	2015	2016
New borrowings	(69)	(1,335)	(1,304)
Repayments	370	104	1,681
Currency effects and consolidation changes	(504)	(425)	(223)
Changes in debt	(203)	(1,656)	154

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 aggregate principal amount of USD bonds. Other changes resulting from consolidation and currency effects led to an increase of EUR 223 million.

In 2015, total debt increased by EUR 1,656 million. New borrowings of EUR 1,335 million were mainly due to a short-term bridging loan with low interest rate used for the Volcano acquisition, while repayments amounted to EUR 104 million. Other changes resulting from consolidation and currency effects led to an increase of EUR 425 million.

At the end of 2016, long-term debt as a proportion of the total debt stood at 72% with an average remaining term of 7.8 years, compared to 71% and 10.7 years at the end of 2015.

For further information, please refer to [note 18, Debt](#).

2.1.20 Shareholders' equity

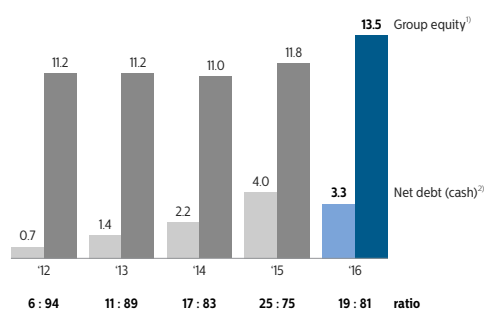
Shareholders' equity increased by EUR 939 million in 2016 to EUR 12,601 million at December 31, 2016. The increase was mainly a result of EUR 1,491 million net income, partially offset by EUR 589 million related to the purchase of shares for the share buy-back program. The dividend payment to shareholders of Koninklijke Philips N.V. in 2016 reduced equity by EUR 330 million including tax and service charges, while the delivery of treasury shares increased equity by EUR 74 million.

The number of outstanding common shares of Royal Philips at December 31, 2016 was 922 million (2015: 917 million). At the end of 2016, the Company held 7.2 million shares in treasury to cover the future delivery of shares (2015: 11.8 million shares). This was in connection with the 33.5 million rights outstanding at the end of 2016 (2015: 39.1 million rights) under the Company's long-term incentive plans. At the end of 2016, the Company did not hold any shares for cancellation (2015: 2.2 million shares). In 2016 Philips purchased call options on Philips shares matching the majority of the options granted to employees until 2013. As of December 31, 2016 Philips held 14.1 million call options as a hedge of 15.9 million remaining options granted to employees.

2.1.21 Net debt to equity

Philips ended 2016 with a position of EUR 3,272 million, compared to a net debt¹⁾ position of EUR 3,994 million at the end of 2015.

Philips Group
Net debt to group equity²⁾ in billions of EUR
 2012 – 2016



¹⁾ Shareholders' equity and non-controlling interests

²⁾ Non-GAAP financial measure. For the definition and reconciliation to the most directly comparable GAAP measure, refer to [chapter 4, Reconciliation of non-GAAP information](#), of this Annual Report

2.1.22 Liquidity position

As of December 31, 2016, including the cash position (cash and cash equivalents), as well as its EUR 2.3 billion committed revolving credit facilities, the Philips Group

had access to available liquidity of EUR 4,634 million vs. Gross Debt (including short and long-term) of EUR 5,606 million.

As of December 31, 2015, including the Company's cash position (cash and cash equivalents), as well as its EUR 1.8 billion committed revolving credit facility, the Company had access to available liquidity of EUR 3,566 million vs. Gross Debt (including short and long-term) of EUR 5,760 million.

Philips Group
Liquidity position in millions of EUR
2014 – 2016

	2014	2015	2016
Cash and cash equivalents	1,873	1,766	2,334
Committed revolving credit facility/CP program/Bilateral loan	1,800	1,800	2,300
Liquidity	3,673	3,566	4,634
Available-for-sale financial assets at fair value	75	75	36
Short-term debt	(392)	(1,665)	(1,585)
Long-term debt	(3,712)	(4,095)	(4,021)
Net available liquidity resources	(356)	(2,119)	(936)

Royal Philips has a EUR 1.8 billion committed revolving credit facility that can be used for general group purposes and as a backstop of its Commercial Paper Programme and will mature in February 2018. 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. There is a panel of banks, in Europe and in the US, which service the program. The interest is at market rates prevailing at the time of issuance of the commercial paper. There is no collateral requirement in the Commercial Paper Programme. Also, there are no limitations on Philips' use of funds from the program. As of December 31, 2016, Royal Philips did not have any loans outstanding under these facilities.

Royal Philips' existing long-term debt is rated Baa1 (with stable outlook) by Moody's and BBB+ (with stable outlook) by Standard & Poor's. Our net debt¹⁾ position is managed in such a way that we expect to retain a strong investment grade credit rating. Furthermore, the Group's aim when managing the net debt¹⁾ position is dividend stability and a pay-out ratio of 40% to 50% of continuing net income. Royal Philips' outstanding long-term debt and credit facilities do not contain financial covenants or cross-acceleration provisions that are based on adverse changes in ratings. A description of Philips' credit facilities, including any covenants, can be found in [note 18, Debt](#).

As at December 31, 2016, Philips had total cash and cash equivalents of EUR 2,334 million. Philips pools cash from subsidiaries to the extent legally and economically feasible. Cash not pooled remains available for local operational or investment needs.

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

In December 2016, Royal Philips delivered a notice of redemption to the holders of the outstanding 5.750% Notes due 2018 in the aggregate principal amount of USD 1,250 million for redemption in January 2017. For further information, refer to [note 31, Subsequent events](#).

2.1.23 Cash obligations

Contractual cash obligations

Presented below is a summary of the Group's contractual cash obligations and commitments at December 31, 2016.

Philips Group
Contractual cash obligations^{1,2)} in millions of EUR
2016

	total	Payments due by period			
		less than 1 year	1-3 years	3-5 years	after 5 years
Long-term debt ³⁾	5,117	1,290	104	1,297	2,426
Finance lease obligations	307	93	127	54	33
Short-term debt	210	210	-	-	-
Operating leases	942	227	300	195	220
Derivative liabilities	841	280	410	-	151
Interest on debt ⁴⁾	2,229	184	306	295	1,444
Purchase obligations ⁵⁾	260	108	73	33	46
Trade and other payables	2,848	2,848	-	-	-
Contractual cash obligations	12,754	5,240	1,320	1,874	4,320

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⁾ Approximately 30% of the debt bears interest at a floating rate.

⁵⁾ Philips has commitments related to the ordinary course of business which in general relate to contracts and purchase order commitments for less than 12 months. In the table, only the commitments for multiple years are presented, including their short-term portion

Philips has no material commitments for capital expenditures.

Additionally, Philips has a number of commercial agreements, such as supply agreements, which provide that certain penalties may be charged to the Company if it does not fulfill its commitments.

Certain Philips suppliers factor their trade receivables from Philips with third parties through supplier finance arrangements. At December 31, 2016 approximately EUR 360 million of the Philips accounts payable were known to have been sold onward under such arrangements whereby Philips confirms invoices.

¹⁾ Non-GAAP financial measure. For the definition and reconciliation to the most directly comparable GAAP measure, refer to [chapter 4, Reconciliation of non-GAAP information](#), of this Annual Report.

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 201 million restructuring-related provisions by the end of 2016, of which EUR 174 million is expected to result in cash outflows in 2017. 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 745 million), in cash or shares at the option of the shareholder, against the net income for 2016. Further details will be given in the agenda for the Annual General Meeting of Shareholders, to be held on May 11, 2017.

Guarantees

Philips' policy is to provide guarantees and other letters of support only in writing. Philips does not provide other forms of support. At the end of 2016, the total fair value of guarantees recognized on the balance sheet amounted to EUR nil (December 31, 2015: EUR nil). Remaining off-balance-sheet business and credit-related guarantees provided on behalf of third parties and associates decreased by EUR 9 million during 2016 to EUR 28 million (December 31, 2015: EUR 37 million).

2.1.24 Analysis of 2015 compared to 2014

The analysis of the 2015 financial results compared to 2014, 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 2016, which will be filed electronically with the US Securities and Exchange Commission.

2.2 Social performance

At Philips we are passionate about improving lives through meaningful innovation. Our people find this aim powerful and inspiring, answering a calling to help create a healthier society. We reflect this aim in all that we do, starting with our people, extending to our stakeholders, as inspiration for new products and services, and through the community work of the Philips Foundation.

Our people

At Philips, we are committed to fostering an ecosystem that inspires inclusion, enables our employees to thrive, and puts our purpose of improving lives at the heart of everything we do. Our people are one of our unique strengths and each one of our employees is instrumental in Philips' success. Our strategy is based

on the belief that every employee at Philips has talent and can grow and contribute with increasing impact. We take great pride in our Philips culture, which is rooted in innovation, R&D and entrepreneurship. We strive to hire employees with backgrounds and perspectives that can mirror the diversity of our markets and customers, fueling insight and innovation across our business.

During 2016 we successfully split Philips Lighting from Royal Philips. This facilitated greater focus and growth in each business, but also necessitated change and adjustment for our people. Throughout this process, our people have demonstrated their significant professionalism in making this a smooth transition, from both a people and business perspective, ensuring moments of uncertainty were supported with care.

2.2.1 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 908 million people in 2016, driven by our Diagnosis & Treatment businesses and Connected Care & Health Informatics businesses. Additionally, our products that help people live a healthy life improved the lives of 324 million people, and our Green Solutions that contribute to a healthy ecosystem 1.74 billion people. After the elimination of double counts – people touched multiple times – we arrived at 2.1 billion lives. This is an increase of around 100 million compared to 2015, driven by all segments, mainly in Greater China, North America, ASEAN, and the Indian subcontinent.

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 www.results.philips.com/interactive-worldmap

The following table shows the Lives Improved metric per market.

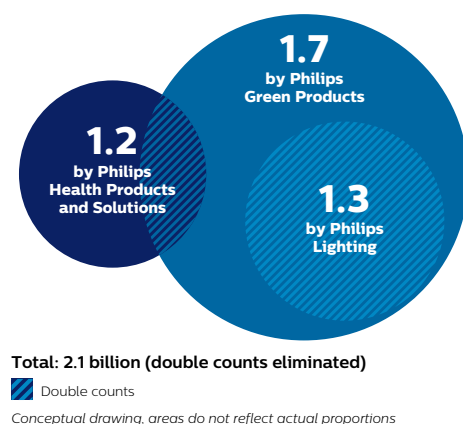
Philips Group			
Lives Improved per market			
Market	Lives Improved (million) ¹⁾	Population (million) ²⁾	GDP (USD billion) ³⁾
Africa	54	1,185	2,186
ASEAN and the Pacific	246	948	5,765
Benelux	28	29	1,301
Central & East Europe	86	125	1,399
Germany, Austria and Switzerland	94	100	4,548
France	60	66	2,519
Greater China	395	1,410	12,851
Iberia	46	57	1,463
Indian subcontinent	213	1,522	2,583
Italy, Israel and Greece	55	82	2,392
Japan	35	127	4,730
Latin America	179	630	5,273
Middle East & Turkey	109	346	2,888
Nordics	26	27	1,460
North America	354	360	20,094
Russia and Central Asia	82	285	1,721
UK & Ireland	51	70	2,973

¹⁾ Source: Philips; double counts eliminated

²⁾ Source: The World Bank, CIA Factbook & Wikipedia

³⁾ Source: IMF, CIA Factbook & Wikipedia

Philips Group
Lives improved in billions

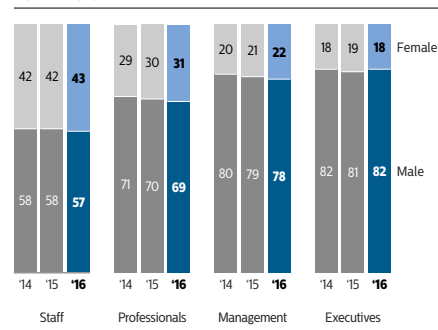


Inclusion requires intentional acceptance; a mindset and workplace where every employee's ideas, knowledge, perspectives, experiences, and styles are valued. The conviction that all individuals should be treated fairly and respectfully, have equal access to opportunities and resources, and can contribute fully to our success.

Data insights

- Gender diversity figures remained stable at 36% overall, with slight increases in the Staff, Professional and Management categories
- Age diversity increased slightly in 2016 with an increase in the under 25 age group
- 120+ nationalities bringing a rich diversity of capabilities, opinions and perspectives
- 47% of our employees are located in growth geographies

Philips Group
Gender diversity in %
2014 – 2016



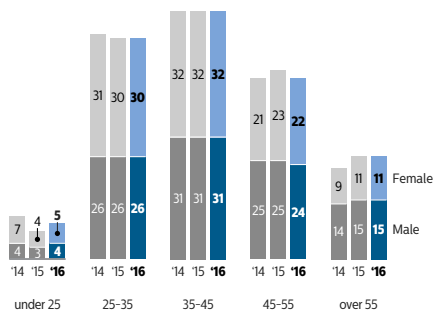
2.2.2 Including, engaging and inspiring our people

The ability to capture growth and seize market opportunities depends on our people – their alignment with our vision, a sense of common purpose, and the belief that their role at Philips is making a positive contribution.

Inclusion and Diversity

Philips recognizes that the best and most innovative solutions are generated through collaboration between people who think differently from one another and genuinely welcome a variety of ideas and viewpoints.

Philips Group
Employees per age category in %
2014 – 2016



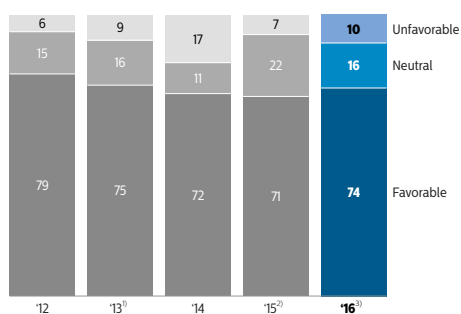
Engagement and Inspiration

Our employee survey consistently reports high levels of employee engagement, above 70% throughout 2010–2016, and rising from 71% to 74% favorable between 2015 to 2016 for the HealthTech businesses. Details on the Lighting employee engagement results can be found in the Philips Lighting Investor Relations [website](#).

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 at home.

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

Philips Group
Employee Engagement Index in %
2012 – 2016



¹⁾ Based on 60 pulse surveys conducted in 2012

²⁾ Based on My Accelerate! Surveys

³⁾ Based on My Accelerate Surveys in HealthTech

2.2.3 Hiring and acquiring our people

In 2016, over 10,000 people were appointed to roles within Philips; 69% of executive vacancies were filled by internal candidates, the remainder were external hires with 60% coming from other healthcare or IT companies. In line with previous years, roughly one third of all roles were filled with internal candidates and the remainder filled with highly qualified external talent.

Three successful integrations were completed in 2016, Volcano, PathXL and Wellcentive, also infusing the organization with additional talent with deep health technology expertise.

Philips' focus on health technology has enabled activation of more highly targeted recruitment campaigns and outreach efforts. As such, Philips has continued to strengthen in-house talent acquisition capabilities, completing 80% of Executive hires in 2016, and saving EUR 3 million in agency costs.

Recruitment campaigns have been customized to raise awareness and attractiveness of Philips as a top healthcare technology employer within critical talent segments, for example Software and Q&R. The [Code to Care](#) campaign achieved 340,000 prospects to the software careers page, supporting 77% growth in digital talent pipelines. Likewise the [Quality Gene](#) campaign resulted in a 35% increase in applications, and a 39% increase in Q&R hires from strategically targeted companies.

In 2016, Philips was recognized as the best-in-class in talent acquisition by [Corporate Executive Board](#) and is in the top 1% of [LinkedIn](#) top global talent attractors. In addition, Best Place to Work programs helped Philips boost attractiveness to passive talent in the labor market in 2016, winning category awards in the United States, Netherlands, Germany, Spain, and Panama.

2.2.4 Employment

The total number of Philips Group employees (continuing operations) was 105,223 at the end of 2016, compared to 104,204 at the end of 2015. Approximately 33% were employed in the Lighting segment, 23% in the Diagnosis & Treatment businesses, 21% in the Personal Health businesses, 13% in the HealthTech Other segment and 10% in the Connected Care & Health Informatics businesses.

Philips Group
Employees per segment in FTEs at year-end
2014 – 2016

	2014	2015	2016
Personal Health	21,488	21,384	22,530
Diagnosis & Treatment	20,104	23,638	23,791
Connected Care & Health Informatics	9,119	10,290	11,033
HealthTech Other	13,019	11,493	13,570
Lighting	41,635	37,399	34,256
Legacy Items			43
Continuing operations	105,365	104,204	105,223
Discontinued operations	8,313	8,755	9,508
Philips Group	113,678	112,959	114,731

Compared to 2015, the number of employees in continuing operations increased by 1,019. The increase reflects insourced manufacturing for products with critical process capability requirements, increased resources in digital innovation across marketing and software, and growth through acquisition. This targeted growth was partially offset by industrial footprint rationalization at Lighting, a reduction of traditional sales roles, and a decrease in operational headcount in central functions.

Approximately 53% of the Philips workforce was located in mature geographies, and about 47% in growth geographies. In 2016, the number of employees in mature geographies increased by 67, mainly due to the Wellcentive acquisition in the Connected Care & Health Informatics segment. The number of employees in growth geographies increased by 952 driven by three factors: Global Business Services right-shoring supporting functions, further shift and rationalization in industrial footprint, and new legislation introduced in China, which capped contingent workforce size at 10% and prompted insourcing of contingent workers.

Philips Group
Employees per geographic cluster in FTEs at year-end
2014 – 2016

	2014	2015	2016
Western Europe	29,105	28,590	28,326
North America	22,283	23,614	23,839
Other mature geographies	3,643	3,908	4,014
Mature geographies	55,031	56,112	56,179
Growth geographies	50,334	48,092	49,044
Continuing operations	105,365	104,204	105,223
Discontinued operations	8,313	8,755	9,508
Philips Group	113,678	112,959	114,731

Philips Group
Employment in FTEs at year-end
2014 – 2016

	2014	2015	2016
Balance as of January 1	116,082	113,678	112,959
Consolidation changes:			
Acquisitions	1,506	1,865	163
Divestments	(247)	(300)	(571)
Changes in Discontinued operations	(2,132)	442	753
Other changes	(1,531)	(2,726)	1,427
Balance as of December 31	113,678	112,959	114,731

In 2016, employee turnover amounted to 16.0% (of which 9.6% was voluntary) compared to 16.6% (9.7% voluntary) in 2015. 2016 turnover was mainly due to the changing industrial footprint in Lighting and our overhead reduction program.

Philips Group
Employee turnover in %
2016

	Staff	Professionals	Management	Executives	Total
Female	21.2	12.1	10.8	13.7	17.0
Male	23.4	10.3	9.3	10.7	15.4
Philips Group	22.4	10.8	9.6	11.2	16.0

Philips Group
Voluntary turnover in %
2016

	Staff	Professionals	Management	Executives	Total
Female	13.0	8.0	7.5	5.9	10.7
Male	13.4	6.3	4.7	4.8	9.0
Philips Group	13.2	6.8	5.3	5.0	9.6

2.2.5 Developing our people

At Philips, we operate with in belief that everyone has talent and that our people are critical to our organizational success. With over 105,000 talented and motivated employees all over the world, it is our people who continue to turn our strategy into reality. Our sustained growth and long-term success will be achieved by becoming a world-class talent-builder, offering attractive and rewarding work which contributes to the careers of our people.

Philips University

In 2016, Philips University began implementing a targeted approach to delivering learning, focusing on strategic needs, identified through strategic plans of the business, strategic workforce planning, and talent reviews. These plans help ensure the effectiveness of our learning budget. Also, innovative learning techniques including gamification, video and micro-learning were infused into learning offerings.

For more information on our people's development, please refer to [sub-section 12.3.2, People development](#), of this Annual Report.

2.2.6 Health and Safety

At Philips we strive to make the world healthier and more sustainable through innovation. A critical aspect of which starts with our own people. We believe we are at our best when our employees are at theirs. A belief championed by our CEO in his recent [Financial Times article](#).

Philips strives for an injury-free and illness-free work environment, with a sharp 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 regret to report two fatalities in Philips Lighting in 2016. One of our sales officers passed away after a traffic accident in Pakistan. In India a contractor died due to injuries sustained at one of our factories. For both of these fatalities, a thorough investigation and root cause analysis were conducted. Corrective actions were implemented, including reminding our employees of safe driving rules and accelerating our injury prevention program to prevent such occurrences in the future.

In 2016, we recorded 174 LWIC, of which 71 in Philips Lighting. These are occupational injury cases where the injured person is unable to work one or more days after the injury. This represents a significant decrease compared with 213 in 2015, and continues the downward trend since 2010. The LWIC rate decreased to 0.18 per 100 FTEs, compared with 0.21 in 2015. The number of Lost Workdays caused by injuries decreased by 1,253 days (16%) to 6,728 days in 2016.

In 2016, we recorded 395 TRC, of which 156 in Philips Lighting. These are cases where the injured employee is unable to work one or more days, or 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 2017.

For more information on Health and Safety, please refer to [sub-section 12.3.4, Health and Safety performance](#), of this Annual Report.

2.2.7 General Business Principles

The Philips General Business Principles (GBP) incorporate the fundamental principles for all Philips business around the world. They set the minimum standard for business conduct for both individual employees and for the company and our subsidiaries. Our GBP also stand as a reference for the business conduct we expect from our business partners and suppliers. Translations of the 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 the GBP in their day-to-day work environments.

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 of these can be found at www.philips.com/gbp.

As part of our unyielding effort to raise GBP awareness and create engagement throughout the organization on the different forms acting with integrity can take, each year a GBP communications and training plan is deployed. In 2016 a number of new initiatives were undertaken through various channels such as our spotlight article series, Quick Reference Cards for at-a-glance guidance on how to handle a number of common GBP concerns as well as returning programs such as e-Learnings which were deployed early in the year. Many of these initiatives contributed to building momentum towards our annual Dialogue Week in the third quarter, which serves as the highlight of our GBP program for the year. During 2016's Dialogue Week hundreds of Philips teams 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 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 after having completed their GBP e-training. In addition, employees in respective specialized areas must sign-off on the Financial and Supply Management Codes of Ethics. Executives are requested to sign-off on the General Business Principles to confirm a renewed commitment to awareness of and compliance with the respective codes each year.

The GBP Review Committee is responsible for the effective deployment of the GBP and for generally promoting a culture of compliance and ethics within Philips. The GBP Review Committee is a body chaired by the Chief Legal Officer, and its members include the Chief HR Officer, the Chief Market Leader and the Chief Financial Officer. They are supported in the implementation of their initiatives by a Committee Secretariat, and a network of GBP Compliance Officers who are appointed in all countries and at all major sites where Philips has operations.

Related roles and responsibilities are laid down in the Charter of the GBP Review Committee. In 2016, in response to external regulatory developments in business ethics and compliance, a revised charter was deployed by the GBP Review Committee. This newly updated charter impacted the composition of the GBP Review Committee, the roles and responsibilities of its

members as well as the composition, roles and responsibilities of the GBP Compliance function. To strengthen monitoring and oversight of GBP compliance within Philips, a mandatory annual GBP self-assessment questionnaire was introduced. 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 equipped with the requisite skills and support to monitor and enhance compliance in the increasingly regulated environments in which Philips operates.

The GBP are supported by established mechanisms that ensure standardized reporting and escalation of concerns. These mechanisms are based on the GBP Reporting Policy that urges employees to report any concerns they may have regarding business conduct in relation to the GBP either through a GBP Compliance Officer or through the Philips Ethics Line. The Philips Ethics Line enables employees and also third parties to report a concern either by telephone or online via a web intake form in a variety of different languages 24/7 all year round. All concerns raised are registered consistently in a single database hosted externally from Philips by a third party and are investigated uniformly in accordance with standardized investigation procedures.

More information on the Philips GBP can be found in [chapter 5, Risk management](#), of this Annual Report. The results of the monitoring measures in place are given in [sub-section 12.3.5, General Business Principles](#), of this Annual Report.

2.2.8 Working with stakeholders

In organizing ourselves around customers and markets, we create 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. To deliver on our vision to make the world healthier and more sustainable through innovation, working with partners is crucial. An overview of stakeholders and topics discussed is provided in [chapter 12, Sustainability statements](#), of this Annual Report.

For more information on our stakeholder engagement activities in 2016, please refer to [sub-section 12.3.7, Stakeholder Engagement](#), of this Annual Report.

2.2.9 Supplier sustainability

Royal Philips has a direct business relationship with approximately 8,500 product and component suppliers and 22,000 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 the stakeholder engagement process are used as an input to develop our supplier sustainability strategy. We then translate this strategy into five dedicated programs:

1. Supplier sustainability compliance

Combination of contractual sustainability commitment of Philips suppliers defined in two core Supplier Sustainability policy documents (Supplier Sustainability Declaration (SSD) and Regulated Substances List (RSL)) and additional transparency requirements to provide information and evidence on topics mentioned in SSD and RSL.

2. Supplier sustainability performance

This program aims to bring about structural, sustainable improvement in our supply chain while focusing on health and safety, remuneration and benefits, and workforce turnover. This approach has been designed to replace the Philips audit program and was piloted in 2016 on a sample of 93 supplier sites in China.

3. Responsible sourcing

This program aims to manage sustainability risks related to minerals mined in conflict-affected and high-risk regions. Philips addresses the complexities of the minerals supply chains through continuous due diligence process combined with multi-stakeholder initiatives to responsible sourcing.

4. Circular procurement

Philips' ambition is to increase its circular business proposition and it has set a 2020 target to achieve 15% circular revenues. This program identifies how procurement can contribute to our ambition to be a provider of circular solutions and services.

5. Environmental footprint China

This program serves to reduce the environmental footprint of our suppliers' sites in China. Furthermore, we want to focus on increasing supply chain transparency in terms of environmental footprint and to drive responsible use of resources through our supply chain. An example is the collaboration of Philips with a Chinese NGO, the Institute of Public Environment (IPE).

Please refer to [sub-section 12.3.8, Supplier indicators](#), of this Annual Report for more details and to the Philips Lighting Investor Relations [website](#) for details on the Lighting Supplier Sustainability program.

2.3 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 Royal Philips 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 new program, as well as the initial results, 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 12, Sustainability statements](#), of this Annual Report and sections [section 2.2, Social performance](#), of this Annual Report and [section 2.3, Environmental performance](#), of this Annual Report. Please refer to [section 12.5, Assurance report of the independent auditor](#), of this Annual Report. With this, Philips is a frontrunner in this field.

Please refer to the Philips Lighting Investor Relations [website](#) for more details on the new Lighting sustainability program and results.

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 12, Sustainability statements](#), of this Annual Report.

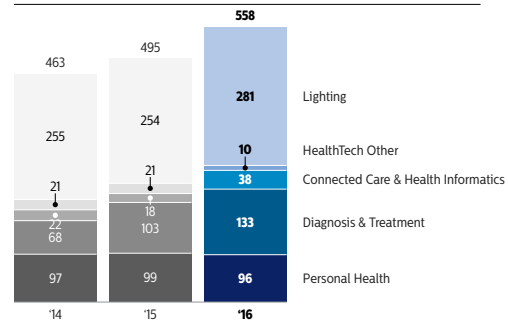
2.3.1 Green Innovation

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 HealthTech businesses over the coming five years as part of the 'Healthy people, sustainable planet' program.

In 2016, Philips invested EUR 558 million in Green Innovation while the HealthTech businesses invested EUR 1.3 billion in Sustainable Innovation.

Philips Group
Green Innovation per segment in millions of EUR
2014 – 2016



Diagnosis & Treatment businesses

Philips develops innovative Diagnosis & Treatment solutions that enable first-time right diagnosis, precision interventions and therapy, while respecting the boundaries of natural resources. Investments in Green Innovation in 2016 amounted to EUR 133 million, a 29% increase compared to 2015. All Philips Green Focal Areas are taken into account while 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. Closing the materials loop is another area where our focus on developing upgrading pathways has enabled extended product life and therefore 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 and outcomes. Investments in Green Innovation in 2016 amounted to EUR 38 million, a doubling compared to 2015. 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 96 million in 2016, compared with EUR 99 million in 2015. 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. In particular, close to 100% of the Mother & Child Care, Male Grooming and Oral Healthcare products are completely PVC/BFR free.

Lighting

Philips Lighting strives to make the world healthier and more sustainable through energy-efficient light. With a 2016 investment of EUR 281 million in Green Innovation, Lighting invested 11% more compared to 2015. Increasing investments in digital solutions and connectivity have led to further improvements in the area of energy efficiency. In 2016, Philip Lighting teamed up with the Dubai Municipality to create the Dubai Lamp Initiative, a unique research partnership that resulted in the development of the world's most energy-efficient commercially available LED lamp. By replacing conventional lamps with the Dubai Lamp – the first commercially available 200 lumen per watt LED lamp – households and enterprises can reduce electricity used for lighting by more than 90% compared to incandescent technologies. In addition to raising light and energy efficiency to new levels, the Dubai Lamp is extremely durable with an average lifespan of up to 15 times that of conventional lamps.

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 the 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. Intellectual Property

& Standards has developed a Sustainable IP portfolio for which the spend has been included in the above total for HealthTech Other.

At the end of 2016, Philips' IP portfolio consisted of 5.7% green patent families. All families are labeled with at least one Green Focal Area. In 2016, 3.3% of our total new patent filings were flagged as relating to green patent family. As IP is an extension of Philips' innovation efforts, the portfolio percentage related to green patents is multiplied by our annual patent portfolio costs to determine Philips' yearly investment in Green IP.

While a product can be classified as green because it incorporates an environmentally friendly technology, such technology cannot always be protected in a patent because of a lack of patentability over the state-of-the-art technology. Therefore, there is not necessarily a correlation between green patents and Green Technologies in Green Products and Solutions.

Circular Economy

The transition from a linear to a circular economy is essential 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.

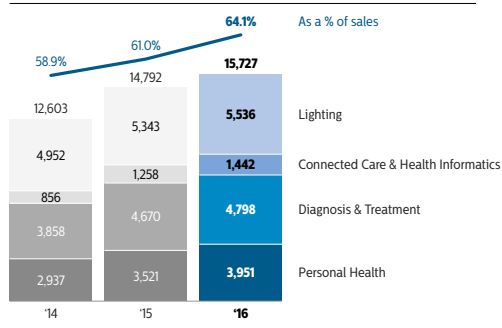
For more information on our Circular Economy activities and the progress towards targets in 2016, please refer to [sub-section 12.4.1, Circular Economy](#), of this Annual Report. Please refer to the Philips Lighting Investor Relations [website](#) for more details on circular products and solutions of Philips Lighting.

2.3.2 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, excluding the Lumileds and Automotive business, increased to EUR 15.7 billion in 2016, or 64.1% of sales (61.0% in 2015), thereby reaching a record level for Philips.

The exclusion of Lumileds and Automotive had a 1% negative impact on the total Green Revenues percentage.

Philips Group
Green Revenues per segment in millions of EUR
 2014 – 2016



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 2016, the latter driven by our Circular Economy initiatives.

New Green Products and Solutions from each segment include the following examples.

Diagnosis & Treatment businesses

In 2016, our Diagnosis & Treatment businesses maintained the 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 continued to add an energy-efficient CryoCompressor to our MRI systems, with energy savings in the various non-scanning modes of 30–40%.

Connected Care & Health Informatics businesses

Our Connected Care & Health Informatics businesses grew the Green Product and Solutions portfolio with three new products and solutions which offer better technology and functionality and at the same time reduce environmental impact. Examples include a new patient monitor GS10/GS20/G30E/G40E series from our Goldway China site with a 21% reduction in product weight and an 18% reduction in energy usage, compared to the predecessor products. Another example is the patient mask AF541, which has a 33% lower product weight and no longer contains polycarbonate compared to its predecessor mask and thus has no risk of containing bisphenol-A.

Personal Health businesses

Our Personal Health businesses focuses 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 2016 surpassed 56% of total sales. All our Green Products with rechargeable batteries (like toothbrushes, shavers, and grooming products) exceed the stringent California energy efficiency norm by at least 10%. We are making steady progress in developing PVC/BFR-free products. More than 55% of 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 product sales, PVC/BFR has already been phased out to a significant extent, but the products are not yet completely free of these substances.

Sleep & Respiratory Care (S&RC) launched the Simple Mini Go portable oxygen concentrator (POC), the smallest and lightest POC ever developed by Philips; compared to its predecessor the product weight has been reduced by 40% and energy efficiency improved by 20%.

Lighting

Green Revenues within Lighting increased to 78% in 2016. Connected Lighting systems and LED contributed to Green Revenues with solutions in more applications and market segments. In Jakarta, Indonesia, 90,000 street luminaires were retrofitted this year with energy efficient LED lights connected by the Philips CityTouch lighting management system. Each light point is now connected, using sensors that collect performance data. As a result, city officials can now monitor Jakarta's lighting infrastructure, remotely managing light levels to match different needs by district. At the same time, Jakarta can better manage its carbon footprint, reduce energy expenses and improve public services.

2.3.3 Sustainable Operations

The Sustainable Operations programs, in Royal Philips and Philips Lighting 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 12, Sustainability statements](#), of this Annual Report.

Carbon footprint and energy efficiency

Both Royal Philips and Philips Lighting are committed to the ambition of becoming carbon-neutral in our operations during the COP21 United Nations Climate Summit in Paris (December 2015). The target we have set is to be 100% carbon-neutral in our operations by 2020 and sourcing all our electricity usage from 100% renewable sources.

After achieving our 40% reduction target in 2015 compared to our 2007 base year we continued to decrease our carbon emissions in 2016. We achieved a 5% carbon reduction compared to 2015, resulting in a total of 1,344 kilotonnes CO₂ emission. This reduction is mainly driven by increasing our renewable electricity share globally from 56% in 2015 to 62% in 2016. This led to a 17% carbon reduction in our industrial sites. As of December 2016 we source 100% of our US electricity demand from the Los Mirasoles windfarm in Texas

through a 15-year Power Purchase Agreement. Additionally, Philips created a renewable electricity purchasing consortium with AkzoNobel, DSM and Google, and the four companies closed the first wind energy transaction in the Netherlands in October 2016 – the Krammer windfarm in the Zeeland province.

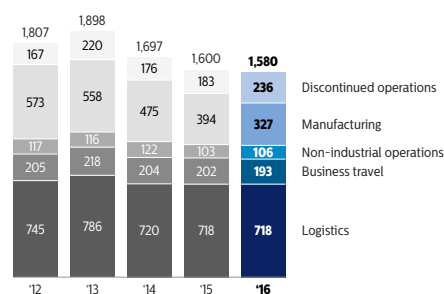
Our business travel emissions showed a reduction of 4% compared to 2015, driven by a stricter air travel policy introduced in the last quarter of 2016. This led to an air travel reduction of 5%. The emissions resulting from our lease cars decreased by 4%, slightly offset by an increase in carbon emissions from our rental cars usage (+6%). In order to further decrease our business travel emissions we will continue to promote video conferencing as an alternative to travel in 2017.

Within our logistics operations we have seen no significant changes in the overall carbon emissions compared to the previous year. Our air freight emissions went up 6% over the course of 2016 to meet demand in our HealthTech businesses, partially caused by distress at one of our larger ocean freight carriers. This was offset by significant reductions within Lighting due to a stricter air freight policy and a Royal Philips program to increase the loading degree of our containers for ocean freight.

Our operational energy efficiency improved by 8%, from 1.11 terajoules per million euro sales in 2015 to 1.01 terajoules per million euro sales in 2016 as a result of energy efficiency programs in our industrial sites. During 2016, 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) 2016 emission factors. Philips reports all its emissions in line with the Greenhouse Gas Protocol (GHGP) as further described in [chapter 12, Sustainability statements](#), of this Annual Report.

The impact of the exclusion of Lumileds and Automotive is displayed as discontinued operations in the next graph; the size of which varies over the years, but averages around 18% over the past five years where emissions from our non-industrial facilities and business travel have been estimated based on FTE data. In 2016, Lumileds and Automotive business travel was based on actuals and non-industrial sites were extrapolated based on floor area. For our logistics emissions, the part of discontinued operations has been estimated using Philips Lighting revenue share as a proxy.

Philips Group
Operational carbon footprint in kilotonnes CO₂-equivalent
2012 – 2016



Philips Group
Operational carbon footprint by Greenhouse Gas Protocol scopes in kilotonnes CO₂-equivalent
2012 – 2016

	2012	2013	2014	2015	2016
Scope 1	355	361	320	261	229
Scope 2 (market based)	335	313	277	236	204
Scope 3	950	1,004	924	920	911
Philips Group	1,640	1,678	1,521	1,417	1,344
Scope 2 (location based)	584	583	546	496	488

Philips Group
Ratios relating to carbon emissions and energy use
2012 – 2016

	2012	2013	2014	2015	2016
Operational CO₂ emissions in kilotonnes CO ₂ -equivalent	1,640	1,678	1,521	1,417	1,344
Operational CO₂ efficiency in tonnes CO ₂ -equivalent per million EUR sales	74	76	71	58	55
Operational energy use in terajoules	30,013	30,890	28,741	26,792	24,824
Operational energy efficiency in terajoules per million EUR sales	1.35	1.40	1.34	1.11	1.01

Water

Total water intake in 2016 was 2.4 million m³, about 11% lower than in 2015. This decrease was mainly due to operational changes, lower production volumes at multiple Lighting sites where water is used for cooling purposes, and water-saving actions at various sites.

Lighting represents around 60% of total water usage. At Lighting, water is used in manufacturing as well as for domestic purposes. In Royal Philips, water is mainly used for domestic purposes. The exclusion of Lumileds and Automotive has a significant downward impact on the water consumption of Philips. In 2016, Lumileds and Automotive accounted for 1.7 million m³ of water.

Philips Group
Water intake in thousands of m³
 2012 – 2016

	2012	2013	2014	2015	2016
Personal Health	368	652	585	614	613
Diagnosis & Treatment	281	311	392	268	269
Connected Care & Health Informatics	75	77	74	94	81
Lighting	2,413	2,249	2,052	1,751	1,451
Continuing operations	3,137	3,289	3,103	2,727	2,414
Discontinued operations	1,720	1,755	1,700	1,684	1,651
Philips Group	4,857	5,044	4,803	4,411	4,065

In 2016, 70% of water was purchased and 30% was extracted from groundwater wells.

Waste

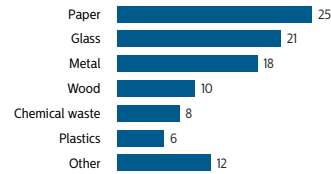
In 2016, total waste decreased by some 5% compared to 2015 to 64.8 kilotonnes, mainly due to operational changes, lower production volumes and less packaging waste at Lighting sites. Lighting contributed 62% of total waste, Personal Health businesses 22%, Diagnosis & Treatment businesses 14% and Connected Care & Health Informatics businesses 2%. The reported increase in waste in Diagnosis & Treatment businesses was partially caused by the removal of obsolete components and two newly acquired reporting sites. The exclusion of Lumileds and Automotive had a downward impact on total waste of 6.2 kilotonnes.

Philips Group
Total waste in kilotonnes
 2012 – 2016

	2012	2013	2014	2015	2016
Personal Health	14.6	13.2	13.1	13.8	14.3
Diagnosis & Treatment	7.4	6.7	6.8	8.0	9.2
Connected Care & Health Informatics	1.1	1.1	1.2	1.4	1.4
Lighting	57.5	54.9	53.9	45.3	39.9
Continuing operations	80.6	75.9	75.0	68.5	64.8
Discontinued operations	7.0	16.1	5.4	6.4	6.2
Philips Group	87.6	92.0	80.4	74.9	71.0

Total waste consists of waste that is delivered for landfill, incineration or recycling. Materials delivered for recycling via an external contractor comprised 54 kilotonnes, which equals 83% of total waste, comparable to 2015. Of the 17% remaining waste, 81% comprised non-hazardous waste and 19% hazardous waste. A total of 6.1 kilotonnes of waste was sent to landfill. Our sites are addressing both the recycling percentage as well as waste sent to landfill as part of both the new Royal Philips and Philips Lighting sustainability programs.

Philips Group
Industrial waste delivered for recycling in %
 2016



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 reduced from 26 kilos in 2015 to 7 kilos in 2016, mainly caused by one site in China which phased out a thinner containing benzene. For the fourth year in a row, mercury emissions at Lighting were as low as reasonably achievable, according to our assessment. The level of emissions of hazardous substances decreased from 25,101 kilos to 12,412 kilos in 2016 (-51%), mainly driven by changes in the lacquering process and product mix in the Personal Health businesses.

Philips Group
Restricted and hazardous substances in kilos
 2012 – 2016

	2012	2013	2014	2015	2016
Restricted substances	67	37	29	26	7
Hazardous substances	67,530	35,118	28,310	25,101	12,412

For more details on emissions from substances, please refer to [sub-section 12.4.3, Sustainable Operations](#), of this Annual Report.

2.4 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 reservations made 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, 2016, 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 745 million), in cash or in shares at the option of the shareholder, against the net income for 2016.

If the above dividend proposal is adopted, the shares will be traded ex-dividend as of May 12, 2017 and May 15, 2017 at the New York Stock Exchange and Euronext Amsterdam, respectively. 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 16, 2017.

Shareholders will be given the opportunity to make their choice between cash and shares between May 17, 2017 and June 9, 2017. If no choice is made during this election period the dividend will be paid in cash. On June 9, 2017 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 June 7, 8 and 9, 2017. 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 13, 2017. Payment of the dividend and delivery of new common shares, with settlement of fractions in cash, if required, will take place from June 14, 2017. 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 12, 2017.

Further details will be given in the agenda for the 2017 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 2016, a dividend of EUR 0.80 per common share was paid in cash or shares, at the option of the shareholder. For 55.0% of the shares, the shareholders elected for a share dividend resulting in the issue of 17,344,462 new common shares, leading to a 1.9% dilution. EUR 330 million was paid in cash. See also [chapter 14, 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, 2016, is before appropriation of the result for the financial year 2016.

3 Segment performance

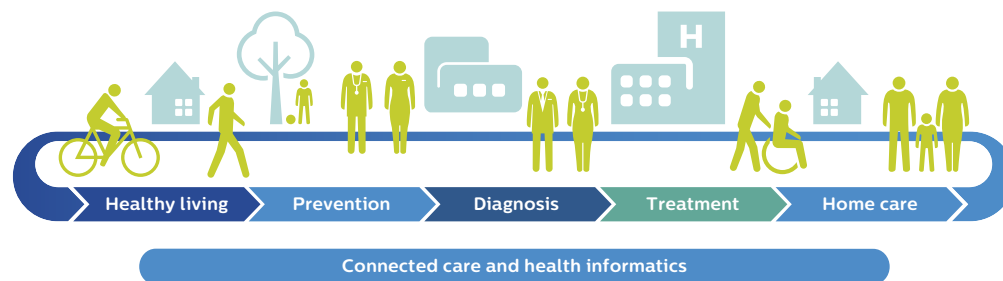
The health technology landscape

Health systems around the world are under increasing economic pressure. More people are living longer, and more are living with chronic conditions – driving healthcare spending to unsustainable levels. Shortages of healthcare professionals are also adding to the relentless challenge of delivering better care at lower cost to growing patient populations.

Fundamental transformative changes are already taking place in the healthcare industry to enable the provision of affordable, quality care to those who need it. A shift is under way towards value-based healthcare, which places greater emphasis on results, driving the reduction of waste and inefficiency, increasing access and improving outcomes, while at the same time reducing costs.

Consumers are becoming increasingly engaged in managing their own health, with greater attention being focused on the benefits of healthy living and home care. Mobile and digital technologies are significant enablers of this trend, leading to new care delivery models – founded upon integrated care, real-time analytics and personalized solutions and services – that give patients greater control over, and responsibility for, their health.

Philips (NYSE: PHG, AEX: PHIA) is a health technology company focused on improving people's lives through meaningful innovation across the health continuum – from healthy living and prevention to diagnosis, treatment and home care. Applying advanced technologies and deep clinical and consumer insights, Philips partners with customers to deliver integrated solutions that enable better outcomes at lower cost.



Our structure in 2016

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 and continued to consolidate Philips Lighting, through 2016. On February 8, 2017, Philips announced that it had successfully completed an accelerated bookbuild offering to institutional investors and to Philips Lighting of 26.0 million shares in Philips Lighting, reducing Philips' stake in Philips Lighting's issued and outstanding share capital from 71.225% to approximately 55.180%. The transaction is in line with Philips' stated objective to fully sell down its stake in Philips Lighting over the next several years.

In light of its focus on health technology, effective January 1, 2016, Philips eliminated the former Healthcare and Consumer Lifestyle sector layers in order to drive the convergence of consumer health and professional healthcare, as well as to reduce overhead costs, and changed the reporting of its health technology activities. At the same time, the former Innovation, Group & Services was split and allocated to Philips and Philips Lighting respectively.

In 2016, Philips' activities in the field of health technology were organized on a segment basis. The reportable segments are Personal Health businesses, Diagnosis & Treatment businesses, Connected Care & Health Informatics businesses and Lighting, each being responsible for the management of its business worldwide. Additionally, Philips identifies HealthTech Other and Legacy Items, as shown below:

Philips					
HealthTech				Lighting	Legacy Items
Personal Health businesses	Diagnosis & Treatment businesses	Connected Care & Health Informatics businesses	Other		
Health & Wellness	Diagnostic Imaging	Patient Care & Monitoring Solutions	Innovation	Lamps	Legacy litigation
Personal Care	Image-Guided Therapy	Healthcare Informatics, Solutions & Services	Emerging Businesses	LED	Separation cost
Domestic Appliances	Ultrasound	Population Health Management	IP Royalties	Professional	
Sleep & Respiratory Care ¹			Central costs	Home	
			Other	Other	

Focus of external reporting

¹⁾ Previously part of the Healthcare sector

At the end of 2016, Philips had 82 production sites in 22 countries, sales and service outlets in approximately 100 countries, and 105,223 employees.

3.1 Personal Health businesses

The Chief Business Leader of the Personal Health businesses segment and Chief Marketing Officer, Pieter Nota, joined Philips in 2010 as CEO of Philips Consumer Lifestyle. Prior to that he was on the Board of Management of Beiersdorf AG as Chief Marketing & Innovation Officer. He started his career at Unilever.

3.1.1 About Personal Health businesses

Our Personal Health businesses play an important role on the health continuum, 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 four main factors:

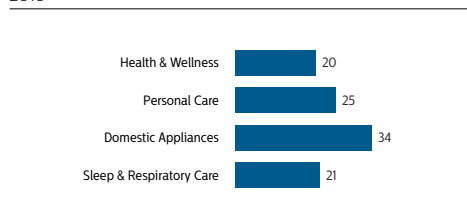
- Innovation at the forefront of digital health, based on deep consumer insights
- Value propositions leveraging consumer data, unlocking recurring revenue streams
- High-impact consumer marketing programs
- Geographical expansion with proven propositions

Through 2016, we have driven above-market growth and are stepping up profitability towards 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 2016, the Personal Health segment consisted of the following areas of business:

- **Health & Wellness:** mother and child care, oral healthcare, pain relief
- **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 %
2016



Through our Personal Health businesses, we offer a broad range of products from high to low price/value quartiles, necessitating a diverse distribution model. 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 are adapting our web functionality to offer consumers a better user experience via smaller screens, driving improvements from conversion to sales. And we continue to roll-out high-impact consumer marketing programs in support of key innovations. The launch of Philips OneBlade, for example, was accompanied by the deployment of an innovative Digital Advocacy Marketing Program.

The company's wide portfolio of connected consumer health products leverages Philips HealthSuite – a cloud-enabled connected health ecosystem of devices, apps and digital tools that enables 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 2016 we launched the Philips Sonicare FlexCare Platinum Connected toothbrush. With unique smart sensor technology inside the toothbrush – connecting to the Philips Sonicare smartphone app via Bluetooth – users receive personalized step-by-step coaching, real-time feedback and post-brush analysis with a visual 3D mouth map to help improve brushing technique. Via the Philips HealthSuite digital platform, the app allows data to be shared with dental practices, so hygienists can mark up areas that need special attention.

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

In 2016, Personal Health employed approximately 22,530 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.

Commitment to quality

The implementation of the Philips Business System is embedding a fundamental commitment to quality across all our processes, products, systems and services. 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 and Personal 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 sourcing, please refer to [sub-section 12.3.8, Supplier indicators](#), of this Annual Report.

3.1.2 2016 business highlights

Philips introduced a range of personalized health programs at this year's IFA trade show in Berlin, including the Philips Sonicare FlexCare Platinum Connected toothbrush and the uGrow medical-grade baby app. The health programs leverage Philips HealthSuite, a cloud-enabled connected health ecosystem of devices, apps and digital tools.

Personal Care successfully launched Philips OneBlade – a hybrid styler that can trim, shave and create clean lines and edges – in France, the UK, Germany and North America.

Sleep & Respiratory Care launched the cloud-based Patient Adherence Management Service, which supports new patients' transition to sleep therapy. Building on the success of the integrated Dream Family solution in the US, Europe and Japan, the Philips DreamStation Go portable CPAP solution was introduced. DreamStation Go is a compact and lightweight device designed to provide sleep therapy for travelers with obstructive sleep apnea.

Oral Healthcare continued its growth trajectory, supported by a strong performance of the Philips Sonicare FlexCare Platinum Connected toothbrush, which has built-in sensor technology that enables real-time feedback and coaching to help consumers optimize their brushing routine.

3.1.3 2016 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
2014 – 2016

	2014	2015	2016
Sales	5,948	6,751	7,099
Sales growth			
% increase, nominal	3%	14%	5%
% increase, comparable ¹⁾	6%	5%	7%
Income from operations (EBIT)	620	736	953
as a % of sales	10.4%	10.9%	13.4%
EBITA ¹⁾	758	885	1,092
as a % of sales	12.7%	13.1%	15.4%

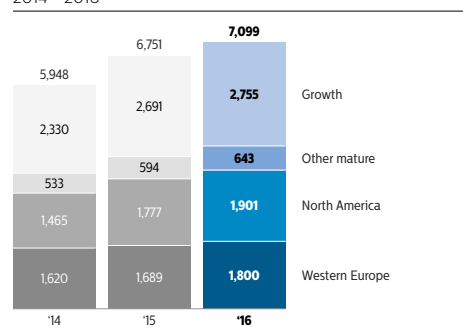
In 2016, sales amounted to EUR 7,099 million, a nominal increase of 5% compared to 2015. Excluding a 2% negative currency impact, comparable sales¹⁾ were 7% higher year-on-year, driven by double-digit growth in Health & Wellness and mid-single-digit growth in Personal Care, Sleep & Respiratory Care and Domestic Appliances. Green Revenues amounted to EUR 3,951 million, or 56% of total segment sales.

From a geographic perspective, on a comparable basis¹⁾ both growth geographies and mature geographies achieved high-single-digit growth. In growth geographies, the increase was mainly driven by Central & Eastern Europe and Middle East & Turkey. Mature geographies recorded high-single-digit growth, driven by high-single-digit growth in Western Europe, mid-single-digit growth in North America and low-single-digit growth in other mature geographies.

Income from operations (EBIT) amounted to EUR 953 million, or 13.4% of sales, which included EUR 139 million of amortization charges, mainly related to intangible assets at Sleep & Respiratory Care.

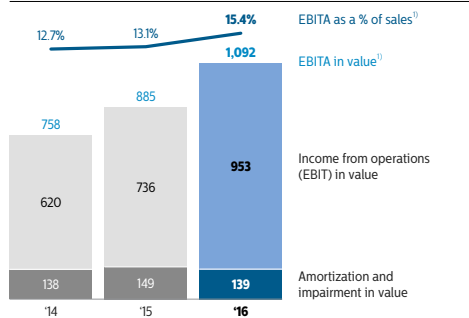
EBITA¹⁾ increased from EUR 885 million, or 13.1% of sales, in 2015 to EUR 1,092 million, or 15.4% of sales, in 2016. Restructuring and acquisition-related charges amounted to EUR 16 million in 2016, compared to EUR 37 million in 2015. EBITA¹⁾ in 2015 also included charges related to the devaluation of the Argentine peso of EUR 13 million. The increase in EBITA¹⁾ was attributable to higher volumes and cost productivity.

Personal Health
Sales per geographic cluster in millions of EUR
2014 – 2016



¹⁾ Non-GAAP financial measure. For the definition and reconciliation to the most directly comparable GAAP measure, refer to [chapter 4, Reconciliation of non-GAAP information](#), of this Annual Report.

Personal Health
Income from operations (EBIT) and EBITA ¹⁾ in millions of EUR
2014 – 2016



¹⁾ Non-GAAP financial measure. For the definition and reconciliation to the most directly comparable GAAP measure, refer to [chapter 4, Reconciliation of non-GAAP information](#), of this Annual Report

waste was recycled. We sent 7% of our manufacturing waste to landfill in 2016 and started a detailed analysis of waste streams that are landfilled by our production sites. Based on this we will define actions to reach our goal of zero waste to landfill in 2020.

3.1.4 Healthy people, sustainable planet

Sustainability continued to play an important role in the Personal Health businesses in 2016, with the main focus on optimizing the sustainability performance of our products and operations. Green Revenues, 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 56% of total sales in 2016. All Green Products with rechargeable batteries exceed the stringent California energy efficiency standard by at least 10%. And over 54% of total 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 1,440 tons of recycled plastics were used in kitchen appliances, vacuum cleaners, irons, air purification and coffee machines, compared to 900 tons in 2015. The revenue from Circular Products reached over EUR 414 million in 2016, comprised of turnover generated from performance- and access-based business models in Sleep & Respiratory Care and products with recycled plastic materials.

As a concrete example of our commitment to sustainability we launched the new Performer Ultimate vacuum cleaner, for which we have created a closed-loop recycling system. Old Philips vacuum cleaners are collected in Western Europe and recycled separately from other products and brands. The plastics from the old vacuum cleaners are then mixed with other recycled plastics to create a new recycled plastic that is used to produce the new Performer Ultimate, which is free of PVC/BFR, has an A-class energy label and contains 36% recycled plastics.

In our operations we continue to draw most of our electricity from renewable sources, with the ultimate aim of having CO₂-neutral production sites by 2020. In 2016, 47% of the electricity used in manufacturing sites came from renewable sources and 85% of the industrial

3.2 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.

3.2.1 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 'triple aim' – to improve outcomes, lower the cost of care delivery and enhance the patient experience – by enabling first-time-right diagnosis and treatment. We are focused on 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 very personalized care. Our informatics platform provides the intelligence to make more consistent decisions, as well as making it easier to share and collaborate.

With our image-guided therapy, clinicians are provided with the technology necessary to determine the presence of disease, guide treatment procedures 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. 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 addition to our solutions for clinical pathways, we provide a range of technologies to help our customers improve their operational results. This year we introduced a comprehensive suite of software services designed to improve radiology department operations – PerformanceBridge is a multi-vendor offering that provides practice management, dose management and service analytics. It can be delivered as a service offering to promote continuous improvement, or as a professional service where our people partner with our customers to improve operating effectiveness.

The value proposition to our 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:

- continuing to improve business fundamentals in Diagnostic Imaging; we made substantial progress in 2016, with, amongst others, the full CT (Computed Tomography) portfolio shipping from Cleveland, Haifa, Suzhou and other facilities
- enhancing our offering in oncology and radiology and expanding our solutions offering, which comprises systems, smart devices, software and services
- leveraging the successful integration of Volcano and driving expansion into devices for treatment
- addressing underpenetrated adjacencies in General Imaging and Obstetrics/Gynecology in Ultrasound

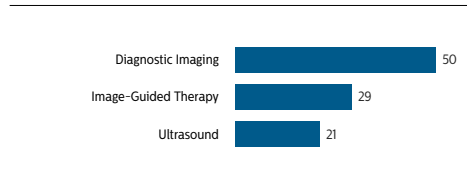
Philips is one of the world's leading health technology companies (based on sales) along with General Electric and Siemens. The competitive landscape in the healthcare industry is evolving with the emergence of new market players. The United States, our largest market, represented 34% of Diagnosis & Treatment's global sales in 2016, followed by China, Japan and Germany. Growth geographies accounted for 33% of Diagnosis & Treatment's sales. In 2016, Diagnosis & Treatment had 23,791 employees worldwide.

Through 2016 we consistently focused on our value-creation strategy to ensure continued growth and margin improvement.

In 2016, the Diagnosis & Treatment segment consisted of the following areas of business:

- **Diagnostic Imaging:** Magnetic Resonance Imaging, Computed Tomography, Diagnostic X-Ray, which includes digital X-ray and mammography, Advanced Molecular Imaging, and integrated clinical solutions, which include radiation oncology 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 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 %
2016



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.

Commitment to quality

The implementation of the Philips Business System is embedding a fundamental commitment to quality across all our processes, products, systems and services. This commitment is of vital importance in the extensively regulated health equipment and system business. We 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.

Further progress was made in 2016 in strengthening the remediated quality management system at our facility in Cleveland, Ohio, with the ramp-up of production and shipments continuing in 2017.

With regard to sourcing, please refer to [sub-section 12.3.8, Supplier indicators](#), of this Annual Report.

3.2.2 2016 business highlights

In line with its strategy of building multi-year strategic partnerships, Philips signed multiple agreements in 2016, including a 10-year EUR 74 million agreement with Russia's Expert Group of Companies to provide solutions combining advanced imaging systems with clinical informatics to improve cardiac care. In China, leveraging its expertise in cardiology, Philips signed a 5-year interventional cardiology solutions agreement with DeltaHealth for the new DeltaHealth Hospital Shanghai, which will specialize in cardiac care. The agreement comprises interventional X-ray systems, ultrasound imaging, software and services.

Within Image-Guided Therapy, Philips Volcano delivered a strong performance with comparable sales growth¹⁾ and continued operational improvements. This was driven by growth across the smart catheter product portfolio, synergies with the Image-Guided Therapy Systems business and expansion in therapy solutions and new geographies.

At RSNA 2016, Philips launched new data-driven, intelligent solutions to improve operational efficiencies and enhance diagnostics and patient care. These include Illumeo Adaptive Intelligence and IntelliSpace Portal 9.0 – advanced informatics and visual analysis solutions with machine-learning capabilities to support the physician.

Leveraging its innovation leadership in diagnostic imaging, Philips has installed the Philips IQon Spectral CT across the globe. The system is the world's first and only spectral detector computed tomography modality that provides clinicians with a comprehensive view of the patient's anatomy, with a single, low-dose examination. Market success is the result of the modality's superb image quality and disease assessment, in particular for oncology.

Demonstrating its continued leadership in ultrasound imaging solutions, Philips received the '2016 Best in KLAS' award in the Ultrasound category. KLAS, a leading global research firm, recognizes companies with the Best in KLAS award for outstanding innovation and contributions to improved patient outcomes based on the past 12 months' performance ratings.

Philips introduced the first commercially available MR-only simulation solution indicated for prostate cancer radiation oncology treatment planning in the United States. The solution is part of Philips' Ingenia MR-RT platform, which supports radiation departments that want to rely on MRI as their primary imaging modality for prostate cancer treatment planning.

3.2.3 2016 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
2014 – 2016

	2014	2015	2016
Sales	5,284	6,484	6,686
Sales growth			
% increase (decrease), nominal	(7)%	23%	3%
% increase (decrease), comparable ¹⁾	(5)%	6%	4%
Income from operations (EBIT)	349	322	546
as a % of sales	6.6%	5.0%	8.2%
EBITA ¹⁾	374	377	594
as a % of sales	7.1%	5.8%	8.9%

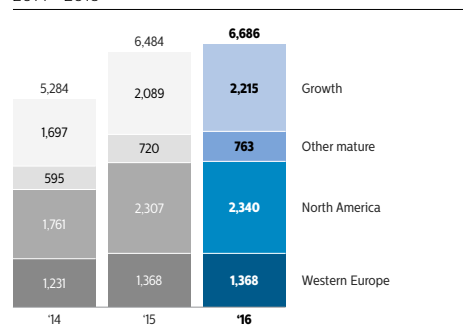
In 2016, sales amounted to EUR 6,686 million, 3% higher than in 2015 on a nominal basis. Excluding a 1% negative currency effect, comparable sales¹⁾ increased by 4%, driven by double-digit growth in Image Guided Therapy, low-single-digit growth in Diagnostic Imaging, while Ultrasound was in line with 2015. Green Revenues amounted to EUR 4,798 million, or 71% of total segment sales.

From a geographic perspective, comparable sales¹⁾ in growth geographies showed double-digit growth, reflecting double-digit growth in Latin America and India and high-single-digit growth in China. Mature geographies were in line with 2015, driven by low-single-digit growth in Western Europe, partly offset by a low-single-digit decline in other mature geographies. North America was in line with 2015.

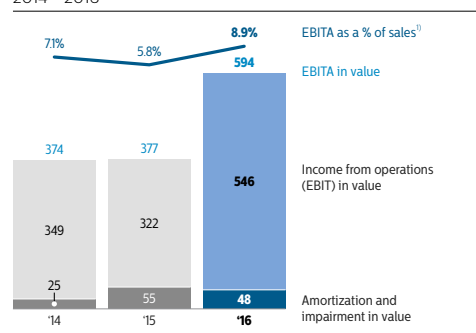
Income from operations (EBIT) amounted to EUR 546 million, or 8.2% of sales, and included EUR 48 million of amortization charges, mainly related to acquired intangible assets in Image-Guided Therapy.

EBITA¹⁾ amounted to EUR 594 million, or 8.9% of sales, compared to EUR 377 million, or 5.8% of sales, in 2015. 2016 included restructuring and acquisition-related charges of EUR 37 million, compared to EUR 131 million in 2015. 2015 also included charges of EUR 7 million related to the devaluation of the Argentine peso. The improvement in margin was driven by Image-Guided Therapy and Diagnostic Imaging, as well as lower restructuring and acquisition-related charges.

Diagnosis & Treatment
Sales per geographic cluster in millions of EUR
2014 – 2016



Diagnosis & Treatment
Income from operations (EBIT) and EBITA¹⁾ in millions of EUR
2014 – 2016



¹⁾ Non-GAAP financial measure. For the definition and reconciliation to the most directly comparable GAAP measure, refer to chapter 4, Reconciliation of non-GAAP information, of this Annual Report

3.2.4 Healthy people, sustainable planet

A growing and aging population, the rise of chronic and lifestyle-related diseases and global resource constraints pose a number of challenges, including pollution and stressed healthcare systems. 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 2016, Green Revenues in Diagnosis & Treatment amounted to EUR 4,798 million thanks to a large portfolio of Philips Green Products and Solutions that support energy efficiency, materials reduction and other sustainability goals. We also actively collaborate with care providers around the globe to look for ways to minimize the environmental impact of healthcare, for example by reducing the energy use of medical equipment.

¹⁾ Non-GAAP financial measure. For the definition and reconciliation to the most directly comparable GAAP measure, refer to chapter 4, Reconciliation of non-GAAP information, of this Annual Report.

Supporting the transition to a circular economy, we have continued to expand the Diamond Select refurbishment program and also the SmartPath upgrading program for all modalities in the Diagnosis & Treatment portfolio.

Philips was presented with the 'Champion for Change' Award by Practice Greenhealth for the third year in a row. This award honors businesses that go beyond taking steps to improve their own green practices, but also help hospitals to expand their sustainable practices.

3.3 Connected Care & Health Informatics businesses

The Chief Business Leader of the Connected Care & Health Informatics businesses segment, Jeroen Tas, has over 30 years of global experience as an entrepreneur and senior executive in the healthcare, information technology and financial services industries. Previously he was CEO of Philips Healthcare Informatics, Solutions & Services, overseeing digital health and clinical informatics, and Group Chief Information Officer (CIO), leading IT worldwide. In February 2017, Jeroen Tas was appointed as Chief Innovation & Strategy Officer and succeeded by Carla Kriwet who joined the Executive Committee as Chief Business Leader of Connected Care & Health Informatics. Carla Kriwet is also the BG Leader of Patient Care & Monitoring Solutions and previously was the Philips Market Leader of Germany, Austria & Switzerland.

3.3.1 About Connected Care & Health Informatics businesses

Spanning the entire health continuum, the Connected Care & Health Informatics businesses aim to empower consumers, care givers and clinicians with digital solutions that facilitate value-based care by enabling precision medicine and population health management, building on Philips' strengths in consumer technology, patient monitoring and clinical informatics.

This requires a common digital framework that connects and aligns consumers, patients, payers and healthcare providers. A framework that aggregates and leverages information from clinical, personal and historic data, using analytics to support care providers in first-time-right diagnosis and treatment, and helps identify the risk and needs of different groups within a population.

To this end we have developed Philips HealthSuite – a cloud-based connected health ecosystem of devices, apps and digital tools. Applying analytics and algorithms, we can use data to deliver predictive, personalized insights, for example to help motivate healthy behavior through digital coaching, to support healthcare professionals in making clinical decisions, or to alert medical teams to potential problems, e.g. with elderly patients living independently at home.

In 2016, the Connected Care & Health Informatics segment consisted of the following areas of business:

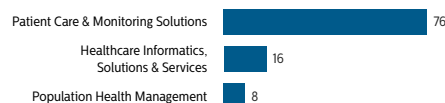
- **Patient Care & Monitoring Solutions:** Enterprise-wide patient monitoring solutions, from value solutions to sophisticated connected solutions, for real-time clinical information at the patient's bedside; patient analytics, patient monitoring and clinical decision support systems including diagnostic 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; and customer service, including clinical, IT, technical, and remote customer propositions.

- **Healthcare Informatics, Solutions & Services** comprises advanced healthcare IT, clinical and advanced visualization and quantification informatics solutions for radiology, cardiology, oncology and neurology departments. It also offers 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. The business group also includes a professional services business (Healthcare Transformation Services) spanning consulting, education, clinical and business performance improvement, program management and system integration services, as well as the Philips HealthSuite digital platform. This platform enables interoperability, data security, big data and predictive analytics, optimized workflows and care pathways, rapid application development, enhanced patient centricity and engagement for the solutions part of the Philips HealthSuite connected health ecosystem.

- **Population Health Management:** Our services and solutions leverage our data, analytics and actionable workflow products, and include: personal health programs (app-based with medical grade measurement devices and coaching) to help people manage their health; technology-enabled monitoring and intervention (telehealth, remote patient monitoring, personal emergency response systems, and care coordination) to improve aging and chronic condition experiences; actionable programs to predict risk (including medication and care compliance, outreach, and fall prediction); and cloud-based solutions for health organizations to manage population health, driving quality improvement and business transformation for those transitioning to value-based care.

Connected Care & Health Informatics
Total sales by business as a %
2016



Sales at Philips' Connected Care & Health Informatics 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.

Commitment to quality

The implementation of the Philips Business System is embedding a fundamental commitment to quality across all our processes, products, systems and services. This commitment is of vital importance in the extensively regulated health equipment and system business. We 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.

Philips' products and related services are subject to various regulations and standards. The Company is committed to quality and over the last years made investments to enable significant progress in this area. The Company is currently in advanced discussions on resolving a civil matter with the US Department of Justice representing the US Food and Drug Administration (FDA), arising from past inspections by the FDA in and prior to 2015. The discussions focus primarily on the Company's compliance with the FDA's Quality System Regulations in the Company's Emergency Care and Resuscitation (ECR) business in the United States. While discussions have not yet concluded, the Company anticipates that the actions necessary to address the FDA's compliance concerns will have a meaningful impact on the operations of its ECR business.

With regard to sourcing, please refer to [sub-section 12.3.8, Supplier indicators](#), of this Annual Report.

3.3.2 2016 business highlights

Philips launched new data-driven, intelligent solutions to improve operational efficiencies and enhance diagnostics and patient care. These include PerformanceBridge, a new suite of operational performance improvement software and services for radiology departments, and Illumeo Adaptive Intelligence and IntelliSpace Portal 9.0, advanced informatics and visual analysis solutions with machine-learning capabilities to support the physician.

Philips acquired Wellcentive, a leading US-based provider of population health management software solutions. Wellcentive complements Philips' portfolio with cloud-based IT solutions to import, aggregate and analyze clinical, claims and financial data across hospital and health systems, to help care providers deliver coordinated care.

In line with its strategy of delivering solutions consisting of smart devices, software and services to address specific customer needs, Philips signed a 3-year patient monitoring solutions agreement with Rush University Medical Center, Chicago. The company also signed a multi-year agreement with the Medical University of South Carolina Health focused on integrated patient monitoring solutions.

Expanding its global leadership in patient monitoring solutions beyond acute care settings, Philips launched the latest version of its IntelliVue Guardian solution in Europe. This solution comprises smart devices including wearable biosensors, clinical decision support software and services. It is designed to aid clinicians in the early recognition of patient deterioration in the hospital's general wards, allowing timely intervention and avoiding adverse events, unplanned transfers back to the ICU and longer lengths of hospitalization.

Building on its expertise in new care models based on telehealth technologies, Philips enabled Macquarie University's MQ Health in Sydney, Australia, and Emory Healthcare in Atlanta, US, to provide continuous nighttime critical care oversight to ICU patients back in Atlanta during daytime hours in Australia.

3.3.3 2016 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
2014 – 2016

	2014	2015	2016
Sales	2,684	3,022	3,158
Sales growth			
% increase (decrease), nominal	(2)%	13%	5%
% increase (decrease), comparable ¹⁾	0%	0%	4%
Income from operations (EBIT)	(157)	173	275
as a % of sales	(5.9)%	5.7%	8.7%
EBITA ¹⁾	(106)	227	322
as a % of sales	(3.9)%	7.5%	10.2%

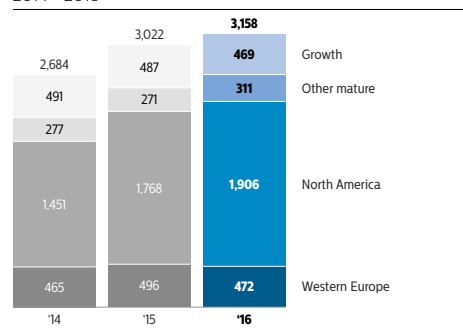
In 2016, sales amounted to EUR 3,158 million, 5% higher than in 2015 on a nominal basis. The 4% increase on a comparable basis¹⁾ was driven by mid-single-digit growth in Patient Care & Monitoring Solutions, low-single-digit growth in Healthcare Informatics, Solutions & Services, partly offset by a low-single-digit decline in Population Health Management. Green Revenues amounted to EUR 1,442 million, or 45% of segment sales.

From a geographic perspective, comparable sales¹⁾ in growth geographies showed high-single-digit growth, and mature geographies recorded low-single-digit growth.

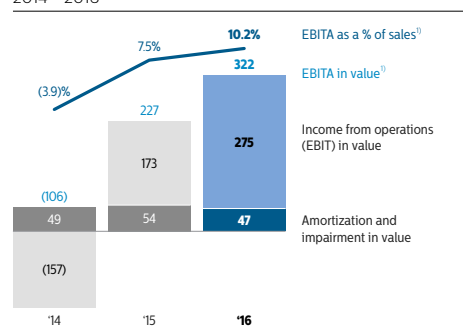
Income from operations (EBIT) amounted to EUR 275 million, or 8.7% of sales, and included EUR 47 million of amortization charges, mainly related to acquired intangible assets at Population Health Management and Patient Care & Monitoring Solutions.

EBITA¹⁾ amounted to EUR 322 million, or 10.2% of sales, compared to EUR 227 million, or 7.5% of sales, in 2015. EBITA¹⁾ in 2016 included restructuring and acquisition-related charges of EUR 14 million compared to EUR 38 million in 2015. 2016 EBITA¹⁾ also included a net release of provisions of EUR 12 million, while in 2015 included charges of EUR 28 million related to the currency revaluation of the Masimo provision and charges of EUR 1 million related to the devaluation of the Argentine peso. The margin increase was mainly driven by higher volumes and lower restructuring and acquisition-related charges and other items, partly offset by higher expenditure on innovation.

Connected Care & Health Informatics
Sales per geographic cluster in millions of EUR
2014 – 2016



Connected Care & Health Informatics
Income from operations (EBIT) and EBITA¹⁾ in millions of EUR
2014 – 2016



¹⁾ Non-GAAP financial measure. For the definition and reconciliation to the most directly comparable GAAP measure, refer to chapter 4, Reconciliation of non-GAAP information, of this Annual Report

3.3.4 Healthy people, sustainable planet

A growing and aging population, the rise of chronic and lifestyle-related diseases and global resource constraints pose a number of challenges, including pollution and stressed healthcare systems. Philips is committed to addressing these challenges 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 solutions can reduce the travel-related carbon footprint of healthcare, and improve access and outcomes.

In 2016, Green Revenues increased to EUR 1,442 million and we continued to expand the portfolio of Philips Green Products that support energy efficiency, materials reduction and other sustainability goals.

Supporting the transition to a circular economy, we continue to expand innovative 'access over ownership' service solutions where our customers pay for things where and when required, while Philips can secure high levels of recycling and materials re-use.

¹⁾ Non-GAAP financial measure. For the definition and reconciliation to the most directly comparable GAAP measure, refer to chapter 4, Reconciliation of non-GAAP information, of this Annual Report.

Philips was presented with the 'Champion for Change' Award by Practice Greenhealth for the third year in a row. This award honors businesses that go beyond taking steps to improve their own green practices, but also help hospitals to expand their sustainable practices.

3.4 HealthTech Other

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

3.4.1 About HealthTech Other

Innovation

At Philips, our innovation efforts are aligned with our business strategy. The Innovation & Strategy function feeds the innovation pipeline, enabling the Philips operating businesses to create new business options through new technologies, new business creation, and intellectual property management and development. Focused research and development improvement activities drive time-to-market efficiency and increased innovation effectiveness.

Innovation & Strategy facilitates innovation from idea to product 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 product development. In addition, it opens up new value spaces beyond the direct scope of current businesses (Emerging Businesses), manages the Company-funded R&D portfolio, and creates synergies for cross-segment initiatives.

Innovation & Strategy includes, among others, the Chief Technology Office and Research, the Chief Medical Office, Innovation Services, Intellectual Property & Standards, Design, Strategy, and Sustainability. Key locations include Eindhoven (Netherlands), Cambridge (USA), Bangalore (India) and Shanghai (China). In total, Innovation & Strategy employs some 5,000 professionals around the globe.

Innovation & Strategy actively participates in Open Innovation through relationships with academic, clinical, and industrial partners, 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.

Research

Research focuses on exploration of new technologies and business ideas, delivering proofs-of-concept and offering consultancy in technology development projects, particularly for first-of-a-kind products and services. It aims to improve people's lives through technology-enabled meaningful innovations – as co-creator and strategic partner of the Philips businesses, markets and Open Innovation ecosystem participants.

Research investigates trends and creates concepts for solutions within strategic Philips domains linked to societal challenges, such as the increase in cardiovascular diseases and cancer, ageing societies, limited access to healthcare and increasing obesity.

The Eindhoven lab is the core lab of Philips Research. It was awarded the Open Innovation 2.0 award from the European Union in 2016 in recognition of its role in creating the High Tech Campus as a vibrant innovation ecosystem.

In the fall of 2015, Philips Research opened a new Innovation Lab in Cambridge, MA (USA), which is now fully up and running. It is home to approximately 100 Philips Research North America employees and another 150 Philips 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.

Philips Research China broadened its scope in 2016 by adding a Digital Innovation team focused on the creation of local digital propositions.

With the aim of extending our capabilities in research for IT healthcare applications, in 2016 we announced our intention to open an R&D site at the Skolkovo Innovation Centre in Moscow, Russia. The new Center will focus on machine learning, artificial intelligence, and computer and data science.

The Philips Africa Innovation Hub in Nairobi, Kenya, creates locally relevant innovations 'in Africa', with particular focus on improving access to affordable healthcare. The Africa Innovation Hub is a collaboration between Philips Research and the Africa market organization. Based on work from this hub, in 2016 Philips and Grand Challenges Canada signed a repayable grant agreement to scale the manufacturing and distribution of the Philips Children's Respiration Monitor (also known as ChARM) to make it affordable and accessible for community-based health workers in low-resource settings throughout the world.

Coming under the Chief Technology Office for reporting purposes, Philips Photonics is 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. Following a significant rise in demand for VCSELs, Philips Photonics announced in 2016 that it would double manufacturing capacity at its laser-diode facility in Ulm, Germany.

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 build 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.

Innovation Services

Innovation Services offers a wide range of expert services in development, realization and consulting. Its skills are leveraged by Philips businesses, markets and Innovation & Strategy in all regions.

Innovation Campus Bangalore

Philips Innovation Campus Bangalore (PIC) hosts activities from most of our operating businesses, Research, Design, IP&S and IT. R&D activities at the PIC include Diagnostic Imaging, Patient Care & Monitoring Solutions, Sleep & Respiratory Care, Personal Health, and Healthcare Informatics, Solutions & Services.

PIC plays a key role in Philips' digital transformation journey. Originally a software center, today PIC is a broad product development center including mechanical, electronics, and supply chain capabilities. PIC works with growth geographies to build market-specific solutions, and several businesses have also located business organizations focusing on growth geographies at PIC.

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 the Philips businesses, Innovation & Strategy, markets and functions, championing a multidisciplinary co-create approach that brings teams together to understand the different factors that influence how a new product or solution will appear, perform and behave.

Increasingly we leverage our design capabilities and processes to work directly with our customers and our customer-facing teams. Innovating directly with our

customers enables Philips Design to deliver people-focused solutions that optimize the user and patient experience and the overall performance of their healthcare systems across the health continuum.

Emerging Businesses

Emerging Businesses is a group dedicated to identifying, developing and bringing to market breakthrough products and services that will help shape the future of healthcare. The group focuses on innovating at the intersection between supportive technologies and current care models that drive improved outcomes, higher patient satisfaction/engagement and reductions in overall cost of care.

One of the businesses is Digital Pathology Solutions, which empowers pathologists with a complete connected digital pathology solution that is designed to optimize productivity and workflow, and ultimately improve the quality of diagnosis. In June 2016, Philips acquired Northern Ireland-based PathXL, an innovator in digital pathology image analysis, workflow software and educational tools, to further expand its Digital Pathology Solutions offering and leadership in Computational Pathology.

Another business is Handheld Diagnostics, with its Minicare proposition launched in May 2016, which provides direct point-of-care diagnostic information at the patient's bedside, enabling physicians to make medical decisions on the spot. Based on innovative technologies, we have designed easy-to-use, patient-centric IVD (in-vitro diagnostics)-enabled solutions and connected services that have the potential to revolutionize health management and improve existing workflows.

A third business is Light & Health, a pioneer in photo dermatology. Leveraging its advanced understanding of the biological effects of light, the team of Philips Light & Health researchers, collaborating with leading research institutions and hospitals, has developed a number of products, for instance Philips BlueControl for treating patients with psoriasis, which feature LED light and offer proven medical benefits.

Finally, a fourth team in Emerging Businesses is working on computational neurology, neuro-mapping and neuro-monitoring.

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 79,000 patent rights, 49,000 trademarks, 86,000 design rights and 4,400 domain names. Philips filed 1,690 patents in 2016, 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.

Philips Design received 158 design awards, including becoming the #1 ranked company in the prestigious international iF ranking for design.

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.

3.4.2 2016 business highlights

Strengthening its Digital Pathology business, Philips acquired PathXL, an innovator in digital pathology image analysis, workflow software and educational tools. Philips also signed a licensing agreement with Visiopharm to offer their breast cancer panel software algorithms with Philips' IntelliSite digital pathology solution to support pathologists in providing an objective diagnosis of breast cancer.

In the 2016 Interbrand annual ranking of the world's most valuable brands, Philips' ranking improved to #41 from #47, with a total estimated brand value of approximately USD 11.3 billion.

Philips rose to first place in the European Patent Office's 2015 ranking of patent applicants for patents filed at the EPO. In addition, the company ranked first in three of the ten leading fields of technology: Medical Technology; Electrical machinery, apparatus, energy; and Measurement.

Building on its commitment to sustainability, Philips launched its new 5-year 'Healthy people, sustainable planet' program to improve the lives of 2.5 billion people per year, increase its Green Revenues to 70% of sales, generate 15% of its sales from Circular Revenues and become carbon-neutral in its operations by 2020.

Philips became the Industry Group Leader in the Capital Goods category in the 2016 Dow Jones Sustainability Index, achieving the highest possible scores in three sections, including climate strategy and operational eco-efficiency.

3.4.3 2016 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 unless otherwise stated
2014 – 2016

	2014	2015	2016
Sales	487	503	478
Income from operations (EBIT)	37	49	(129)
EBITA of: ¹⁾			
IP Royalties	299	284	286
Emerging businesses	(38)	(63)	(98)
Innovation	(92)	(118)	(127)
Central costs	(105)	(31)	(173)
Other	(13)	(8)	(8)
EBITA ¹⁾	51	64	(120)

In 2016, sales amounted to EUR 478 million and reflected EUR 38 million lower royalty income due to the foreseen expiration of licenses, partly offset by new patent license agreements and strong double-digit growth in Emerging Businesses.

In 2016, income from operations (EBIT) totaled to EUR (129) million compared to EUR 49 million in 2015. EBITA¹⁾ amounted to a net cost of EUR 120 million, compared to net gain of EUR 64 million in 2014. EBITA¹⁾ in 2016 included restructuring and acquisition-related charges of EUR 28 million and a EUR 26 million impairment of real estate assets. EBITA¹⁾ in 2015 included a net restructuring release of EUR 19 million and a EUR 37 million gain related to the sale of real estate assets. The year-on-year decrease was mainly attributable to higher restructuring and acquisition-related charges and other items, investments in Emerging Businesses, brand campaigns and cyber security.

3.5 Lighting

Philips Lighting is led by Eric Rondolat, who has held the position of Chief Executive Officer since the company was listed on the Euronext Amsterdam stock exchange (ticker symbol: LIGHT) on May 27, 2016. Prior to that, he was Chief Executive Officer of Lighting at Royal Philips from April 2012 to May 27, 2016.

Following the listing of Philips Lighting, Philips retained a 71.225% stake and continued to consolidate Philips Lighting through 2016, with the aim of fully selling down over the next several years. On February 8, 2017, Philips announced that it had successfully completed an accelerated bookbuild offering to institutional investors and to Philips Lighting of 26.0 million shares in Philips Lighting, reducing Philips' stake in Philips Lighting's issued and outstanding share capital from 71.225% to approximately 55.180%. The transaction is in line with Philips' stated objective to fully sell down its stake in Philips Lighting over the next several years.

3.5.1 Lighting landscape

A number of trends and transitions are affecting the lighting industry and changing the way people use and experience light.

Philips Lighting serves a large and attractive market that is driven by the need for more light, the need for energy-efficient lighting, and the need for digital and connected lighting.

The world's population is forecast to grow from 7 billion today to over 10 billion by 2050. At the same time, we are witnessing rapid urbanization, with about two-thirds of the world's population expected to live in urban areas by 2050. These trends will increase demand for light. In addition, in the face of resource constraints and climate change, the world needs that light to be energy-efficient. At the same time, the lighting industry is moving from conventional to LED lighting, which is changing the way people use, experience and interact with light. Digital technologies enable connectivity and seamless integration in software architectures, systems and services. Connected lighting allows light points to be used as information pathways, opening up new functionalities and services based on the transmission and analysis of data.

3.5.2 About Lighting

Philips Lighting is a global market leader with recognized expertise in the development, manufacture and application of innovative, energy-efficient lighting products, systems and services that improve people's lives. It has pioneered many of the key breakthroughs in lighting over the past 125 years, laying the basis for its current strength and leading position in the digital transformation to connected lighting.

Philips Lighting has a firm strategy which is based upon six priorities:

- Optimize cash from conventional products to fund our growth
- Innovate in LED products commercially and technologically to outgrow the market
- Lead the shift to systems, building the largest connected installed base
- Capture adjacent value through new services business models
- Be our customers' best business partner locally, leveraging our global scale
- Accelerate! on our operational excellence improvement journey

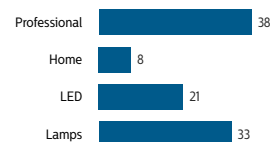
The work Philips Lighting did in 2016 saw it extend its lighting leadership into the Internet of Things and allowed it to unlock new experiences and value for customers. It announced many connected lighting innovations, and new customers and partnerships, for street lighting, retail, offices and homes.

The company aims to further invest to support its leadership in LED and connected lighting systems and services while at the same time capitalizing on its broad portfolio, distribution and brand in conventional lighting by successful implementation of its 'last man standing' strategy.

Philips Lighting addresses people's lighting needs across a full range of market segments. Indoors, it offers lighting products, systems and services for homes, shops, offices, schools, hotels, factories and hospitals. Outdoors, it offers products, systems and services for roads, streets, public spaces, residential areas and sports arenas, as well as solar-powered LED off-grid lighting. In addition, it addresses the desire for light-inspired experiences through architectural projects. Finally, it offers specific applications of lighting in specialized areas, such as entertainment, horticulture, and water purification.

In 2016, Philips Lighting spanned a full-service lighting value chain – from lamps, luminaires, electronics and controls to connected and application-specific systems and services – through the business groups Lamps, LED, Professional and Home.

Lighting
Total sales by business as a %
2016



Philips Lighting is one of the few companies in the world to offer solutions across the lighting value chain – including software, controls, luminaires, light sources, and modules. It will build on its global reach with current commercial activities that cover approximately 180 countries. Philips Lighting has operational manufacturing plants in 22 countries in all major regions of the world, and more than 70 sales offices worldwide.

Commitment to quality

The implementation of the Philips Business System is embedding a fundamental commitment to quality across all Philips Lighting's processes, products, systems and services. Lighting is subject to significant regulatory requirements in the markets where it operates. These include 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-related Products (ErP) and Energy Performance of Buildings (EPBD) directives.

3.5.3 2016 business highlights

Philips Lighting is actively building partnerships for its connected lighting systems for both professional and consumer markets. The company announced a partnership with US company Aisle411 for digital mapping of retail stores. It also teamed up with Amazon Alexa, Google Home and with Huawei's OceanConnect for the interoperability of the Philips Hue connected lighting system, making this the first connected lighting system that can be used with all leading smart home platforms.

Philips Lighting's partnership with Cisco resulted in Power-over-Ethernet connected lighting systems for the headquarters of Smartworld in Dubai, Intel's new research campus in Bangalore and Infinorsa's Torre Europa building in Madrid.

In the retail segment Philips Lighting implemented its first connected lighting indoor positioning system in the Middle East with United Arab Emirates-based retailer aswaaq, one of the world's most innovative supermarkets and community malls. The new system uses lights that act as a positioning system and allows customers to use smartphones to access location-based services.

Philips Lighting also extended the number of connected street lighting contracts, supplying nearly 90,000 connected street luminaires in Jakarta as one of its biggest projects to date. The system will be managed by the Philips CityTouch street lighting management system, which has been installed in more than 700 projects across 35 countries since its inception in 2012.

The range of LED lighting was extended with Philips SceneSwitch, which combines multiple light settings in one lamp, enabling users to select the right light for their

needs using an existing wall switch. It also introduced a range of spots and decorative bulbs that use WarmGlow for dimming, meaning the more you dim, the warmer the light effect. With Dubai Municipality the company developed the Dubai lamp, the world's most energy-efficient commercially available lamp. This family of six lamps and two spots covers 80% of the light sockets in the city.

The company broadened the appeal of its Philips Hue connected lighting system for the home by adding an innovative motion sensor, which allows users to switch their Philips Hue lights on and off simply by walking in or leaving a room.

The Philips Hue range was also extended with Philips Hue white ambiance, providing users with every shade of white light.

Philips Lighting expanded the number of sports stadiums using its Philips ArenaVision dynamic LED pitch lighting, adding the Amsterdam Arena, the Juventus Stadium in Turin, the Volkswagen Arena in Wolfsburg and the indoor stadium in Cairo. The company also provided pitch, façade and office lighting for Atletico Madrid. Philips Lighting is responsible for the pitch lighting of over 65% of stadiums involved in major international sports events.

3.5.4 2016 financial performance

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

Lighting
Key data in millions of EUR unless otherwise stated
2014 – 2016

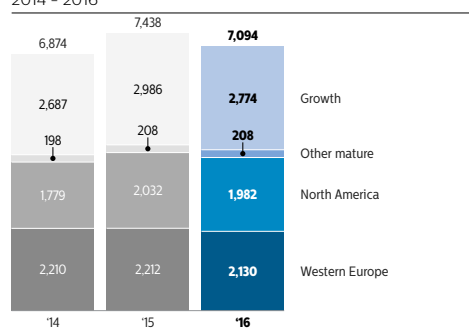
	2014	2015	2016
Sales	6,874	7,438	7,094
Sales growth			
% increase (decrease), nominal	(4)%	8%	(5)%
% increase (decrease), comparable ¹⁾	(3)%	(3)%	(2)%
Income from operations (EBIT)	25	334	432
as a % of sales	0.4%	4.5%	6.1%
EBITA ¹⁾	133	441	542
as a % of sales	1.9%	5.9%	7.6%

In 2016, sales amounted to EUR 7,094 million, 5% decrease on a nominal basis. Excluding a 3% negative currency effect and portfolio changes, comparable sales¹⁾ decreased by 2%, reflecting double-digit growth in LED and Home, a low-single-digit decline Professional and a double-digit decline in Lamps. Green Revenues amounted to EUR 5,536 million, or 78% of total segment sales.

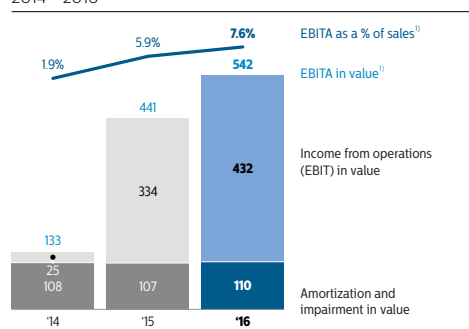
Income from operations (EBIT) amounted to EUR 432 million, or 6.1% of sales, which included EUR 110 million of amortization charges, mainly related to acquired intangible assets at Professional.

EBITA¹⁾ increased from EUR 441 million, or 5.9% of sales, in 2015 to EUR 542 million, or 7.6% of sales in 2016. Restructuring and acquisition-related charges were EUR 119 million, compared to EUR 97 million in 2015. EBITA¹⁾ in 2016 also included a gain of EUR 14 million related to a release of provisions originating from the separation activities. EBITA¹⁾ in 2015 also included EUR 14 million of charges related to the devaluation of the Argentine peso. The increase was mainly attributable to cost reduction programs and an increase in gross margin, partly offset by higher restructuring and acquisition-related charges.

Lighting
Sales per geographic cluster in millions of EUR
2014 – 2016



Lighting
Income from operations (EBIT) and EBITA¹⁾ in millions of EUR
2014 – 2016



¹⁾ For a reconciliation to the most directly comparable GAAP measures, see chapter 4, Reconciliation of non-GAAP information, of this Annual Report

3.5.5 Brighter Lives, Better World

During Climate Week NYC, Eric Rondolat launched Philips Lighting's new sustainability program 'Brighter Lives, Better World', building on the long legacy of Philips' EcoVision programs. The new program is built on two pillars: Green Revenues and Sustainable operations. With 78% of 2016 sales coming from sustainable products, systems and services (72% in 2015), Green Revenues reached a record level for Philips Lighting.

In 2016, approximately 15% of the world's electricity is still being used for lighting. Through its digital LED technology, Philips Lighting offers light that is up to 80% more energy-efficient than conventional technologies, which are still commonly used globally. For this reason, the company has pledged to cumulatively sell 2 billion LED light bulbs by 2020, for which it has already sold 628 million units thus far. In addition, Philips Lighting effectively reduced its operational carbon footprint year-on-year by 20%, also increasing the share of renewable electricity to 67%. Its solutions to effectively reduce, recycle, and re-use the waste in its sites as much as possible resulted in 85% of its total industrial waste being recycled, as part of its journey towards zero waste to landfill.

3.5.6 Separation of Lighting

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. Before the listing of Philips Lighting on Euronext in May 2016, a stand-alone structure was established for Philips Lighting within the Philips Group, effective February 1, 2016. To effectuate the separation and to provide a framework for the relationship between the two companies after the separation, Philips and Philips Lighting entered into a separation agreement and a set of ancillary agreements (collectively, the "Separation Agreement"). The Separation Agreement allocated assets, liabilities, employees and contracts of the Philips Group between the current groups of Philips and Philips Lighting. The separation was guided by the principle that the Philips Lighting group comprises substantially all of Philips' former lighting business, related assets and liabilities, employees and contracts, as well as allocated activities from the former Innovation, Group & Services sector. Furthermore, certain historical exposures and liabilities of the Philips Group were allocated to each of the groups of Philips and Philips Lighting, which are unrelated to their respective businesses.

Upon the listing of Philips Lighting in May 2016, Philips and Philips Lighting also entered into a relationship agreement (the "Relationship Agreement") to manage the continuing relationship between Philips Lighting and Philips as a large shareholder of Philips Lighting upon such listing. The Relationship Agreement will terminate when the stake of Philips falls below 10% (with the exception of certain specific provisions).

¹⁾ Non-GAAP financial measure. For the definition and reconciliation to the most directly comparable GAAP measure, refer to chapter 4, Reconciliation of non-GAAP information, of this Annual Report.

3.6 Legacy Items

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

3.6.1 2016 financial performance

Legacy Items
Key data in millions of EUR unless otherwise stated
 2014 – 2016

	2014	2015	2016
Separation costs		(183)	(152)
Other	(388)	(439)	(43)
Income from operations (EBIT)	(388)	(622)	(195)

Income from operations (EBIT) mainly included EUR 152 million of charges related to the separation of the Lighting business, a EUR 14 million charge related to provisions originating from the separation of the Lighting business, EUR 9 million of costs of addressing legacy issues related to environmental provisions, EUR 4 million of pension costs, EUR 36 million of stranded costs related to the combined Lumileds and Automotive businesses, EUR 11 million of charges related to various provisions, as well as a EUR 46 million gain from the settlement of a pension-related claim. Income from operations (EBIT) in 2015 included EUR 345 million of settlements mainly related to pension de-risking.

4 Reconciliation of non-GAAP information

Koninklijke Philips N.V. (the 'Company') believes that an understanding of sales performance, capital efficiency, financial strength and its funding requirements is enhanced by introducing certain Non-GAAP measures, such as Comparable sales growth, Adjusted income from operations / EBITA and Net debt. In this chapter these measures are further explained and reconciled to GAAP measures.

Non-GAAP measures referred to in this report are cross referenced to this chapter.

Comparable sales growth

Comparable sales exclude the effects of currency movements and changes in consolidation. As indicated in the [note 1, Significant accounting policies](#), sales and income are translated from foreign currencies into the Company's reporting currency, the euro, at the exchange rate on transaction dates during the respective years. As a result of significant currency

movements during the years presented, the effects of translating foreign currency sales amounts into euros could have a material impact. Therefore, these impacts have been excluded in arriving at the comparable sales in euros. Currency effects have been calculated by translating previous years' foreign currency sales amounts into euros at the following year's exchange rates in comparison with the sales in euros as historically reported. The years under review were characterized by a number of acquisitions and divestments, as a result of which 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 contributed to a venture that is not consolidated by the Company, relevant sales are excluded from impacted prior-year periods. Similarly, when an entity is acquired, relevant sales are excluded from impacted periods.

Philips Group
Sales growth composition per segment in %
2014 – 2016

	nominal growth	currency effects	consolidation changes	comparable growth
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
HealthTech Other	(5.0)	0.0	0.0	(5.0)
Lighting	(4.6)	2.1	0.2	(2.3)
Philips Group	1.1	1.4	0.2	2.7
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
HealthTech Other	3.3	(0.3)	(1.9)	1.1
Lighting	8.2	(8.5)	(2.2)	(2.5)
Philips Group	13.3	(9.4)	(1.7)	2.2
2014 versus 2013				
Personal Health	3.0	2.7	0.2	5.9
Diagnosis & Treatment	(6.6)	1.5	0.5	(4.6)
Connected Care & Health Informatics	(2.2)	1.7	0.3	(0.2)
HealthTech Other	(8.5)	0.0	(3.7)	(12.2)
Lighting	(3.9)	2.2	(1.0)	(2.7)
Philips Group	(2.7)	2.0	(0.2)	(0.9)

Philips Group
Sales growth composition per geographic cluster in %
 2014 – 2016

	nominal growth	currency effects	consolidation changes	comparable growth
2016 versus 2015				
Western Europe	0.0	1.6	0.2	1.8
North America	2.1	(0.3)	(0.1)	1.7
Other mature geographies	7.9	(5.5)	(0.4)	2.0
Mature geographies	2.0	(0.2)	0.0	1.8
Growth geographies	(0.5)	4.6	0.4	4.5
Philips Group	1.1	1.4	0.2	2.7
2015 versus 2014				
Western Europe	3.9	(1.9)	(0.7)	1.3
North America	21.2	(18.4)	(1.4)	1.4
Other mature geographies	11.7	(5.3)	(3.7)	2.7
Mature geographies	13.1	(10.2)	(1.4)	1.5
Growth geographies	13.8	(7.9)	(2.4)	3.5
Philips Group	13.3	(9.4)	(1.7)	2.2
2014 versus 2013				
Western Europe	(0.3)	(0.4)	(0.2)	(0.9)
North America	(3.0)	0.9	0.3	(1.8)
Other mature geographies	(5.6)	4.7	0.0	(0.9)
Mature geographies	(2.2)	0.8	0.1	(1.3)
Growth geographies	(3.7)	4.4	(0.7)	0.0
Philips Group	(2.7)	2.0	(0.2)	(0.9)

EBITA

The Company uses the terms EBIT and EBITA to evaluate the performance of the Philips Group and its operating segments. The term EBIT has the same meaning as Income from operations and the term EBITA has the same meaning as Adjusted income from operations. EBITA represents income from operations before amortization and impairment on intangible assets (excluding software and capitalized development expenses). Referencing EBITA is considered appropriate as the Company uses it as one of its strategic drivers to increase profitability through re-allocation of its resources towards opportunities

offering more consistent and higher returns and it will make the underlying performance of our businesses more transparent as it will not be distorted by the unpredictable effects of future, unidentified acquisitions.

EBITA is not a financial measure in accordance with IFRS. Below is a reconciliation of 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
Net income to EBITA in millions of EUR
 2014 – 2016

	Philips Group	Personal Health	Diagnosis & Treatment	Connected Care & Health Informatics	HealthTech Other	Lighting	Legacy Items
2016							
Net Income	1,491						
Discontinued operations, net of income taxes	(416)						
Investments in associates, net of income taxes	(13)						
Income tax expense	327						
Financial expenses	569						
Financial income	(76)						
Income from operations (EBIT)	1,882	953	546	275	(129)	432	(195)
Amortization of intangible assets ¹⁾	350	139	48	47	9	108	(1)
Impairment of goodwill	3	-	-	-	-	2	1
EBITA	2,235	1,092	594	322	(120)	542	(195)
Sales	24,516	7,099	6,686	3,158	478	7,094	
<i>EBITA as a % of sales</i>	<i>9.1%</i>	<i>15.4%</i>	<i>8.9%</i>	<i>10.2%</i>		<i>7.6%</i>	
2015							
Net Income	659						
Discontinued operations, net of income taxes	(245)						
Investments in associates, net of income taxes	(30)						
Income tax expense	239						
Financial expenses	467						
Financial income	(98)						
Income from operations (EBIT)	992	736	322	173	49	334	(622)
Amortization of intangible assets ¹⁾	380	149	55	54	15	107	-
Impairment of goodwill	-	-	-	-	-	-	-
EBITA	1,372	885	377	227	64	441	(622)
Sales	24,244	6,751	6,484	3,022	503	7,438	
<i>EBITA as a % of sales</i>	<i>5.7%</i>	<i>13.1%</i>	<i>5.8%</i>	<i>7.5%</i>		<i>5.9%</i>	
2014							
Net Income	411						
Discontinued operations, net of income taxes	(190)						
Investments in associates, net of income taxes	(62)						
Income tax expense	26						
Financial expenses	415						
Financial income	(114)						
Income from operations (EBIT)	486	620	349	(157)	37	25	(388)
Amortization of intangible assets ¹⁾	332	138	25	50	14	106	(1)
Impairment of goodwill	3	-	-	1	-	2	-
EBITA	821	758	374	(106)	51	133	(389)
Sales	21,391	5,948	5,284	2,684	487	6,874	
<i>EBITA as a % of sales</i>	<i>3.8%</i>	<i>12.7%</i>	<i>7.1%</i>	<i>(3.9)%</i>		<i>1.9%</i>	

¹⁾ Excluding amortization of software and product development.

Net debt

Net debt is defined as the sum of long- and short-term debt minus cash and cash equivalents. The net debt position as a percentage of the sum of group equity (shareholders' equity and non-controlling interests)

and net debt is presented to express the financial strength of the Company. This measure is used by Treasury management of the Company and investment analysts and is therefore included in the disclosure.

Philips Group

Composition of net debt and group equity in millions of EUR unless otherwise stated
2014 – 2016

	2014	2015	2016
Long-term debt	3,712	4,095	4,021
Short-term debt	392	1,665	1,585
Total debt	4,104	5,760	5,606
Cash and cash equivalents	1,873	1,766	2,334
Net debt¹⁾	2,231	3,994	3,272
Shareholders' equity	10,867	11,662	12,601
Non-controlling interests	101	118	907
Group equity	10,968	11,780	13,508
Net debt and group equity	13,199	15,774	16,780
Net debt divided by net debt and group equity (in %)	17%	25%	19%
Group equity divided by net debt and group equity (in %)	83%	75%	81%
Net debt and group equity ratio	17.83	25.75	19.81

¹⁾ Total debt less cash and cash equivalents

5 Risk management

5.1 Our approach to risk management

The Executive Committee, supported by the Risk Management Support Team, oversees and manages enterprise risk. 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. Management is the primary responsible for identifying the critical risks and for the implementation of appropriate risk responses.

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 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 5.2, 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 16, Forward-looking statements and other information](#), of this Annual Report and the overview of risk factors described in [section 5.2, 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. The Risk Management Support Team supports management by assessing the Enterprise Risk profile and continuously working to improve the enterprise risk management framework. Structured risk assessments take place according to the Philips process standard for managing risk.

Philips' risk management process 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 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 timeously to market circumstances. Philips is prepared to take considerable strategic risks 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.
- Operational risks include adverse unexpected 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). Philips aims to minimize downside risks due to the need for high quality of its products and services, reliable IT systems and sustainability commitments.
- Compliance risks cover unanticipated failures to implement, or comply with, appropriate laws, regulations, policies and procedures. Philips has a zero tolerance policy towards non-compliance in relation to breaches of its General Business Principles.
- Financial risk include risks related to Treasury, Accounting and Reporting, Pensions and Tax. Philips is prudent with regard to financial risks and the risk appetite is described in various chapters of this annual report, including [note 30, Details of treasury / other financial risks](#).

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

Corporate Governance

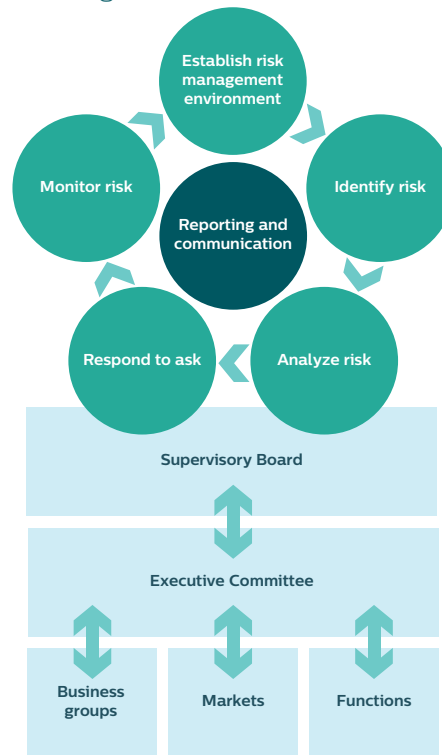
Corporate governance is the system by which a company is directed and controlled. Philips believes that good corporate governance is a critical factor in achieving business success. Good corporate governance derives from, among other things, effective internal controls and high ethical standards. The 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 risk-based operational audits, inspections of financial reporting controls and compliance audits.

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. These Audit & Risk committees are also involved in company-wide internal audit planning as approved by the Audit Committee of the Supervisory Board. 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 9, 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 2016, several risk management workshops were held.

Risk diagram



Key elements of the Philips risk management process 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 12, 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 Supervisory Board.

Examples of measures taken to further strengthen the risk management framework include:

- Definition and execution of the Enterprise Risk Management (ERM) improvement roadmap;
- Process standardization for Risk Management, Internal Control, Compliance and Audit processes as part of the Philips Excellence Process Framework (PEPF) to drive efficiency and continuous improvement;
- The establishment of an Information Security Office and Program in light of the increasing exposure to cybercrime and information security requirements resulting from digitalization and a focus on the Healthcare industry;
- The development of risk management related to long-term strategic partnership given the growing importance of service-based business models.

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 Supervisory Board quarterly.

As part of the Annual Report process, management's accountability for business controls is enforced through the formal issuance of a Statement on Business Controls and a Letter of Representation 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 10.1, Management's report on internal control](#), of this Annual Report.

Philips General Business Principles

The Philips General Business Principles (GBP) incorporate the fundamental principles for all Philips businesses around the globe. They set the minimum standard for business conduct, both for individual employees and for the company and our subsidiaries. Our GBP also stand as a reference for the business conduct we expect from our business partners and suppliers. Translations of the 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 the GBP in their day-to-day work environments.

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.

As part of our unyielding effort to raise GBP awareness and create engagement throughout the organization, each year a GBP communications and training plan is deployed. In 2016, a number of new initiatives were undertaken through various channels such as Quick Reference Cards for at-a-glance guidance on how to handle a number of common GBP concerns, as well as returning programs such as e-Learnings for selected high-risk audiences. Many of these initiatives contributed to building momentum toward our now annual GBP Dialogue Week in October. During 2016's Dialogue Week, hundreds of Philips teams 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 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 after completing their GBP e-training. In addition, employees in the respective specialized areas must sign off on the Financial and Supply Management Codes of Ethics. Executives are requested to sign off on the GBP each year to reaffirm their awareness of and compliance with them.

The GBP Review Committee is responsible for the effective deployment of the GBP and for generally promoting a culture of compliance and ethics within Philips. The GBP Review Committee is chaired by the Chief Legal Officer, and its members include the Chief HR Officer, the Chief Market Leader and the Chief Financial Officer. They are supported in the implementation of their initiatives by a Committee Secretariat, and a network of GBP Compliance Officers, who are appointed in all markets, countries and at all major sites where Philips has operations.

Related roles and responsibilities are laid down in the Charter of the GBP Review Committee. In 2016, in response to external regulatory developments in business ethics and compliance, a revised charter was deployed by the GBP Review Committee. This newly updated charter impacted the composition of the GBP Review Committee, the roles and responsibilities of its members as well as the composition, roles and responsibilities of the GBP Compliance function. To strengthen monitoring and oversight of GBP compliance within Philips, the mandatory annual GBP self-assessment questionnaire, part of our Internal Control framework, was completely renewed. 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 equipped with the requisite skills and support to monitor and enhance compliance in the increasingly regulated environments in which Philips operates.

The GBP are supported by established mechanisms that ensure standardized reporting and escalation of concerns. These mechanisms are based on the GBP Reporting Policy that urges employees to report any concerns they may have regarding business conduct in relation to the GBP, either through a GBP Compliance Officer or through the Philips Ethics Line. The Philips Ethics Line 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. All concerns raised are registered consistently in a single database hosted outside Philips by a third party and are investigated systematically in accordance with standardized investigation procedures.

Financial Code of Ethics

The Company recognizes that its businesses have responsibilities within the communities in which they operate. 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 2016.

For more information, please refer to [sub-section 2.2.7, General Business Principles](#), of this Annual Report.



5.2 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 5.1, Our approach to risk management](#), of this Annual Report. As a result of this process, amongst others, the following actions were performed during 2016:

- Philips completed the separation of its Lighting business and subsequently listed Philips Lighting on the Amsterdam stock exchange and sold a portion of its ownership. This separation has eliminated the separation risk discussed in the 2015 Annual Report. 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.
- The challenging global political and economic developments had an impact on our results. Even though the management of risks related to these developments has not changed compared to 2015, we continuously monitor the impact on our risk profile.

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.

5.3 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 and/or Lighting industries, 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 revenues and income.](#)

Philips' business environment is influenced by political and economic conditions in individual and global markets. Philips experienced the impact from changes in macro-economic development in various geographies during 2016. Economic growth in China was markedly lower compared to average growth over the last two decades. The economic growth of countries which are highly dependent on revenues from energy, raw materials and commodities remains adversely affected by the slowdown of growth in China, most strongly in emerging market countries. Low revenues from oil also affected countries in the Middle East where public spending has been dramatically reduced. Monetary interventions by the European Central Bank did not result in any increase of inflation nor in stronger economic growth in the European Union in 2016. The consensus economic outlook for Great Britain as well as for the European Union has become less favorable as a result of the Brexit vote in June 2016. Although the US economy continued to perform well during 2016, the result of the US presidential election and potential changes in US economic and monetary policies (i.e. expected further rate hikes) may have an impact not only on US dollar but also on a range of emerging market currencies. Both Brexit and the policies of the

new US administration may have significant impact on international trade tariffs and customs laws. The disparate macroeconomic outlook for the main geographies, political conflicts and the unknown impact of Eurozone monetary policy continue to create uncertainty 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. These economic conditions may have an adverse effect on financial markets, which could affect the ability of Philips to make strategic divestments at reasonable price levels or within a reasonable period of time.

The general global political environment remains unfavorable for the business environment due to a rise in political conflicts and terrorism. Numerous other factors, such as sustained lower levels of energy and raw material prices, regional political conflicts in the Middle East, Turkey, Russia and Ukraine 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. The new US administration may implement changes in, among others, US foreign policy, healthcare, 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 rest of the European Union. Elections in a number of key European countries during 2017, which could trigger additional exits from the European Union, may have a similar adverse impact. 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. 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 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 operating results.

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

The risk profile of Philips will change as and when Philips Lighting is sold and deconsolidated. The risk profile is expected to shift towards risks generally associated to Health Technology companies.

Philips' overall performance in the coming years is expected to depend on the realization of its growth ambitions 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 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 and Philips Lighting are examples of companies in which Philips may continue to have a significant (residual) interest but may 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.

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 unforeseen 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.

5.4 Operational risks

[Failure to comply with quality standards and regulations 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 highest 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 such 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 production process). As a result, depending on the product and manufacturing site concerned and the severity of the objection, 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.

[Philips has observed a global increase in IT security threats and higher levels of sophistication in computer crime, posing a risk to the confidentiality, availability and integrity of data and information.](#)

The global increase in security threats and higher levels of professionalism in computer crime have increased the importance of effective IT security measures, including proper identity management processes to protect against unauthorized systems access. Nevertheless, Philips' systems, networks, products, solutions and services remain vulnerable to attacks, which could lead to the leakage of confidential information, improper use of its systems and networks or defective products, which could in turn have a material adverse effect on Philips' financial condition and operating results. In recent years, the risks that we and other companies face from cyber-attacks have increased significantly. The objectives of these cyber-attacks vary widely and may include, among things, disruptions of operations including provision of services to customers or theft of intellectual property or other sensitive information belonging to us or other business partners. 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 customers and partners. Furthermore, enhanced protection measures can involve significant costs. Although we have experienced cyber-attacks and to date have 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 damages 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.

Transformation programs

In 2011, Philips began a transformation program (Accelerate!) designed to unlock Philips' full potential. In 2014, as a next phase in the Accelerate! transformation program, Philips announced its plan to sharpen its strategic focus by establishing two stand-alone companies focused on the HealthTech and Lighting opportunities respectively. The Lighting business was separated in 2016, with Philips selling a portion of its ownership stake and Philips Lighting becoming listed on the Amsterdam Stock Exchange.

Failure to achieve the objectives of any transformation program may have a material adverse effect on the mid-term and long-term financial targets.

In addition, any transformation program in relation to the Finance function may expose Philips to adverse changes in the quality of its systems of internal control.

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 changes. 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.

Businesses purchase raw materials, including so-called rare earth metals, copper, steel, aluminum, noble gases and oil-related products, which exposes them 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 achieve improvements 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, health and safety, environmental and chemical management. Reputational damage could materially impact Philips' brand value, financial condition and operating results.

5.5 Compliance risks

Philips is exposed to non-compliance with product safety laws and data privacy.

Philips' brand image and reputation would be adversely impacted by non-compliance with various product safety laws 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 by various government agencies, including the FDA (US) and comparable foreign agencies. 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. For example the voluntary suspension in 2014 of new production at our Healthcare facility in Cleveland, Ohio targeted to further strengthen manufacturing process controls after certain issues in this area were identified during an ongoing FDA inspection.

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 increasingly 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.

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 25, 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 (See also [note 25, Contingent assets and liabilities](#)).

[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.

5.6 Financial risks

[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 down part of its ownership in Philips Lighting. 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. During this process Philips may lose control over Philips Lighting and deconsolidate the assets, liabilities and financial results of Philips Lighting.

[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 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' supply chain is exposed to fluctuations in energy and raw material prices. Commodities such as oil are subject to volatile markets and significant price increases from time to time. If Philips is not able to compensate for, or pass on in good time, its increased costs to customers, such price increases could have an adverse impact on its 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 30, Details of treasury / other financial risks](#).

[Philips is exposed to tax uncertainties, which could have a significant financial impact.](#)

Philips is exposed to tax uncertainties, which could result in double taxation, penalties and interest payments. These include transfer pricing uncertainties on internal cross-border deliveries of goods and services, tax uncertainties related to acquisitions and divestments, tax uncertainties related to the use of tax credits and permanent establishments, tax uncertainties relating to tax loss and tax credits carried forward and potential changes in tax law that could result in higher tax expenses and payments. The

uncertainties 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 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 on 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 (net) tax losses and credits carried forward will be realized.

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 the sale of Lumileds.](#)

On January 22, 2016, Philips announced the termination of its agreement with GO Scale Capital to sell a stake of 80.1% in Lumileds due to the inability to mitigate regulatory concerns in the US. Philips subsequently engaged with other parties and on December 12, 2016, Philips announced that it had signed an agreement to sell an 80.1% interest in Lumileds to certain funds managed by affiliates of Apollo Global Management, LLC. Subject to regulatory approvals and completion of other closing obligations

Philips expects to receive cash proceeds, before tax and transaction-related costs, of approximately USD 1.5 billion and participating preferred equity. As part of the agreement, Philips will retain a 19.9% interest in the equity of Lumileds by means of common shares for a minimum period of three years following completion of the transaction, subject to the customary drag-along and tag-along conditions or an IPO. There are no voting rights associated with the participating preferred equity held by Philips.

[Philips is exposed to a number of reporting risks.](#)

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.