

# Report on the performance of the Philips Group

- all amounts in millions of euros unless otherwise stated
- the data included in this report are unaudited
- financial reporting according to US GAAP



*'Safe Harbor' Statement under the Private Securities Litigation Reform Act of 1995*

This document contains certain forward-looking statements with respect to the financial condition, results of operations and business of Philips and certain of the plans and objectives of Philips with respect to these items (including, but not limited to, cost savings) in particular the outlook paragraph in this report. By their nature, forward-looking statements involve risk and uncertainty because they relate to events and depend on circumstances that will occur in the future. There are a number of factors that could cause actual results and developments to differ materially from those expressed or implied by these forward-looking statements. These factors include, but are not limited to, levels of consumer and business spending in major economies, changes in consumer tastes and preferences, changes in law, the performance of the financial markets, pension costs, the levels of marketing and promotional expenditures by Philips and its competitors, raw materials and employee costs, changes in exchange and interest rates (in particular, changes in the euro and the US dollar can materially affect results), changes in tax rates and future business combinations, acquisitions or dispositions and the rate of technological changes. Market share estimates contained in this report are based on outside sources such as specialized research institutes, industry and dealer panels, etc. in combination with management estimates. Rankings are based on sales unless otherwise stated.

#### *Use of Non-GAAP Information*

In presenting and discussing the Philips Group's financial position, operating results and cash flows, management uses certain non-GAAP financial measures. These non-GAAP financial measures should not be viewed in isolation as alternatives to the equivalent GAAP measure and should be used in conjunction with the most directly comparable US GAAP measure(s). Unless otherwise indicated in this document, a discussion of the non-GAAP measures included in this document and a reconciliation of such measures to the most directly comparable US GAAP measure(s) is contained in the Annual Report 2003, 'Financial Statements and Analysis'.

## Philips reports net profit of EUR 1,172 million including net gains on IPOs of EUR 743 million

### The third quarter 2004

Philips recorded net income of EUR 1,172 million (EUR 0.92 per share), compared with net income of EUR 124 million (EUR 0.10 per share) in the same period last year.

Sales amounted to EUR 7,229 million, an increase of 3% over the same period last year. The weaker US dollar and dollar-related currencies had a downward effect of 5%. Comparable sales increased by 8%.

Income from operations was a profit of EUR 1,019 million, including a non-taxable gain of EUR 635 million related to the initial public offering of NAVTEQ. In Q3 2003, income from operations was a loss of EUR 126 million. This included EUR 208 million for restructuring and impairment charges.

Unconsolidated companies contributed EUR 337 million to net income, including a gain of EUR 108 million related to the initial public offering of LG.Philips LCD. In Q3 2003, results from unconsolidated companies amounted to EUR 239 million, which included a net dilution gain of EUR 53 million.

Cash flow from operating activities was EUR 292 million. In Q3 2003, cash flow from operating activities totaled EUR 376 million. Inventories as a percentage of sales amounted to 13.4%, the same level as in Q3 2003.

### Gerard Kleisterlee, Philips' President and CEO:

"Q3 was another solid quarter for Philips, with results improving across a broad front. In fact, we would be pleased if it were not for Consumer Electronics, where product margins, especially in Flat TV and DVD+RW, came under heavy pressure in a highly competitive consumer market. These tough market conditions make the quick recovery of margins in Domestic Appliances and Personal Care look even more impressive. Medical Systems, Lighting and Semiconductors all performed well based on product innovation and operating efficiency. The launch of our new brand promise and the creation of a new business unit for Consumer Health and Wellness underline our commitment to drive growth and profitability through our transformation into a Healthcare, Lifestyle and Technology company."

## Highlights in the quarter

### Net income

in millions of euros unless otherwise stated

	Q3 2003	Q3 2004
Sales	6,989	7,229
Income from operations	(126 )	1,019
as a % of sales	(1.8 )	14.1
Financial income and expenses	(24 )	(70 )
Income taxes	54	(97 )
Results unconsolidated companies	239	337
Minority interests	(3 )	(17 )
Cumulative effect of change in accounting principle	(16 )	0
<b>Net income</b>	<b>124</b>	<b>1,172</b>
Per common share – basic	0.10	0.92

### Net income

- Net income totaled EUR 1,172 million, compared with net income of EUR 124 million in the same quarter of 2003. The increase reflected gains on the IPOs of NAVTEQ and LG.Philips LCD as well as improved income from operations.
- Income from operations was a profit of EUR 1,019 million, compared with a loss of EUR 126 million in Q3 2003, an increase of EUR 1,145 million. A gain of EUR 635 million was recognized following the NAVTEQ IPO. Insurance settlements of EUR 61 million were recorded in respect of property and business interruption damage at Semiconductors. Restructuring charges totaled EUR 58 million, compared with EUR 208 million last year. Pension costs were EUR 41 million, compared with EUR 110 million in Q3 2003.
- Results from unconsolidated companies were boosted by the gain of EUR 108 million related to the IPO of LG.Philips LCD.

### Sales by sector

in millions of euros unless otherwise stated

	Q3 2003	Q3 2004	% change	
			nominal	comparable
Medical Systems	1,413	1,408	0	5
DAP	466	450	(3 )	0
CE	2,208	2,280	3	7
Lighting	1,088	1,105	2	7
Semiconductors	1,252	1,388	11	14
Miscellaneous	562	598	6	17
<b>Philips Group</b>	<b>6,989</b>	<b>7,229</b>	<b>3</b>	<b>8</b>

### Sales by sector

- Nominal sales for the Group were 3% higher than last year. Adjusted for the 5% downward effect of the weaker US dollar and dollar-related currencies, sales rose 8%.
- The 5% increase in comparable sales at Medical Systems was driven by double-digit growth of Computed Tomography, Magnetic Resonance and X-Ray. At Domestic Appliances and Personal Care (DAP), increased sales at Food & Beverage were offset by lower sales at Oral Healthcare and Home Environment Care. The 7% sales growth at Consumer Electronics (CE) was driven by Connected Displays, Mobile Infotainment and Licenses. At Lighting, sales growth was visible in almost all businesses and was driven by innovation. Semiconductors showed comparable growth of 14%, the main driver being Mobile Communications.

### Sales per region

in millions of euros unless otherwise stated

	Q3 2003	Q3 2004	% change	
			nominal	comparable
Europe/Africa	2,880	2,980	4	4
North America	1,987	1,879	(5 )	3
Latin America	312	392	26	38
Asia Pacific	1,810	1,978	9	15
<b>Philips Group</b>	<b>6,989</b>	<b>7,229</b>	<b>3</b>	<b>8</b>

### Sales per region

- In Europe/Africa, all sectors except Consumer Electronics posted growth, with Semiconductors leading with a 14% comparable increase. Eastern Europe posted comparable growth of 27%.
- In North America, the weaker dollar had an 8% negative effect on sales. The 3% comparable growth was mainly driven by Semiconductors and Lighting.
- In Latin America, all sectors – especially Consumer Electronics – contributed to the 38% comparable sales growth.
- In Asia Pacific, all sectors showed comparable growth.

## Income (loss) from operations by sector

in millions of euros unless otherwise stated		
	Q3 2003	Q3 2004
Medical Systems	138	164
DAP	82	82
CE	(32)	(15)
Lighting	124	142
Semiconductors	(191)	186
Miscellaneous	(107)	573
Unallocated	(140)	(113)
<b>Income (loss) from operations</b>	<b>(126)</b>	<b>1,019</b>
<b>as a % of sales</b>	<b>(1.8)</b>	<b>14.1</b>

## Income from operations by sector

- Medical Systems' income from operations increased by EUR 26 million, due to higher sales volumes and improved margins.
- Income from operations at DAP equaled the level achieved in 2003 despite lower nominal sales.
- Income from operations at CE improved by EUR 17 million compared to Q3 2003 due to higher license income and cost savings, largely offset by a faster-than-expected decline in gross margins.
- Lighting's strong improvement reflects growth through innovation and solid cost control.
- The substantial improvement in income from operations at Semiconductors was attributable to the continued strong performance of Standard Products and Mobile Communications, as well as the benefits of earlier restructurings and an insurance settlement.
- In Miscellaneous, income from operations was boosted by the successful IPO of NAVTEQ, which yielded a non-taxable gain of EUR 635 million.

## Financial income and expenses

in millions of euros		
	Q3 2003	Q3 2004
Interest expenses (net)	(90)	(66)
Income (loss) from non-current financial assets	65	(1)
Other	1	(3)
<b>Total</b>	<b>(24)</b>	<b>(70)</b>

## Financial income and expenses

- Net interest expense decreased by EUR 24 million, benefiting from the lower level of debt.

## Results unconsolidated companies

in millions of euros		
	Q3 2003	Q3 2004
LG.Philips LCD: operational	131	95
IPO	0	108
LG.Philips Displays	(16)	20
Dilution gains (losses)	53	(10)
Others	71	124
<b>Total</b>	<b>239</b>	<b>337</b>

## Results relating to unconsolidated companies

- A EUR 108 million net gain related to the IPO of LG.Philips LCD was recognized in this quarter.
- LG.Philips Displays posted a sequential income improvement, partly due to a gain on the sale of land and buildings.

## Cash balance

in millions of euros

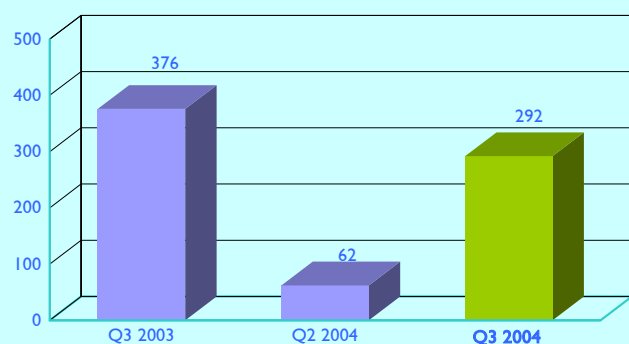
	Q3 2003	Q3 2004
Beginning balance	1,493	2,434
Net cash from operating activities	376	292
Gross capital expenditures	(264)	(263)
Acquisitions/divestments	(76)	367
Other cash from investing activities	174	60
Dividend paid	-	-
Changes in debt/other	(820)	(1,280)
Ending balance	883	1,610

## Cash balance

- The NAVTEQ IPO resulted in a cash inflow of EUR 672 million.
- Cash flow used for acquisitions included an equity contribution to LG.Philips Displays (EUR 202 million) and investments in the Philips-Neusoft Medical Systems joint venture and Gemini (CE investment in the USA).
- During Q3 a repayment of EUR 1 billion was made on a maturing bond. In addition, as part of the effort to manage excess liquidity, EUR 300 million was used for the repurchase of notes maturing August 30, 2005.

## Cash flows from operating activities

in millions of euros

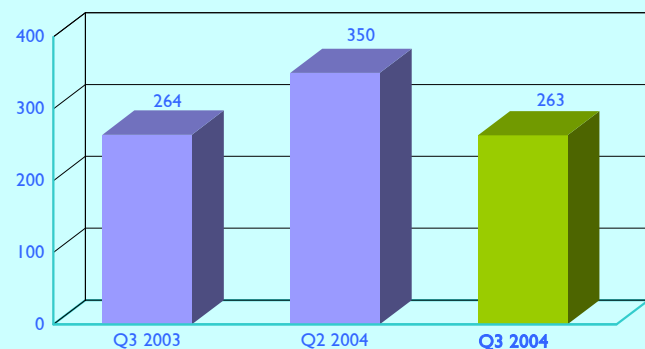


## Cash flows from operating activities

- The decrease in cash flow from operating activities compared with Q3 2003 was due to increased investment in working capital, partly offset by higher income.

## Gross capital expenditures

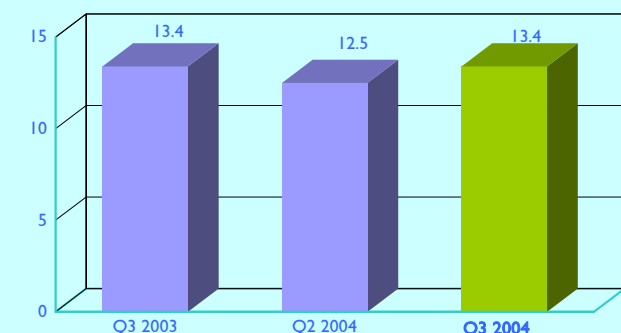
in millions of euros



## Gross capital expenditures

- Gross capital expenditures of EUR 263 million were in line with last year, with increases at Semiconductors and Lighting being offset by declines in other product divisions.
- Gross capital expenditure totaled EUR 117 million at Semiconductors and EUR 54 million at Lighting.
- Compared to Q2, gross capital expenditures were EUR 87 million lower, mainly due to a decrease at SSMC.

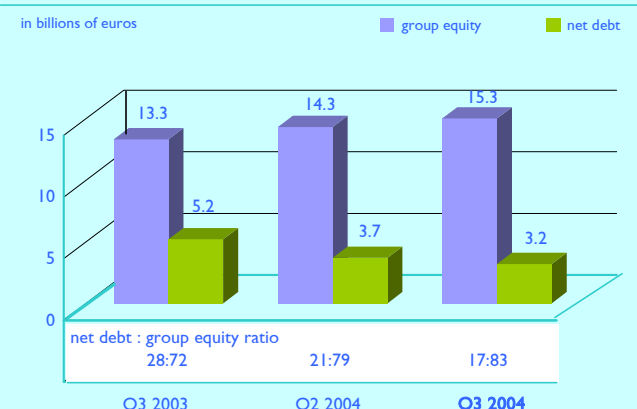
## Inventories as a % of sales



## Inventories

- Inventories as a percentage of sales amounted to 13.4%, the same level as in Q3 2003.
- Compared to last year, improved inventory levels were visible at DAP and Medical Systems, whereas levels increased at Consumer Electronics.

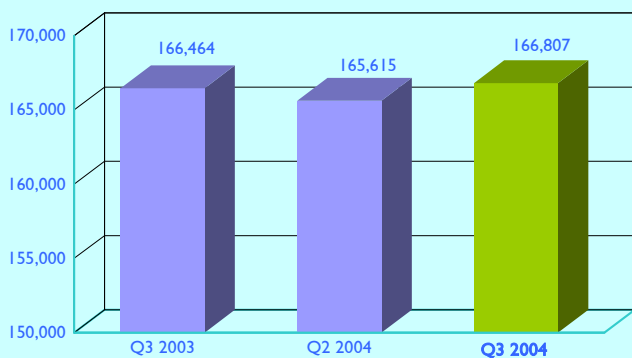
## Net debt and group equity



## Net debt and group equity

- Net debt decreased by EUR 0.5 billion during the quarter mainly due to positive cash flow from operating activities, as well as the proceeds from the sale of NAVTEQ shares, partly offset by an equity contribution to LG.Philips Displays.
- Compared with Q2 2004, group equity increased by EUR 1.0 billion.

## Number of employees (FTEs)



## Employment

- During Q3 the number of employees increased by 1,192, all of them temporary employees. The headcount increase was spread across all sectors except Semiconductors.
- The deconsolidation of NAVTEQ and the consolidation of the newly established Philips-Neusoft Medical Systems joint venture and Gemini led to a decrease in headcount of 491.
- Compared to Q3 2003, the number of employees increased by 343. The headcount increase at Semiconductors (higher level of activity and consolidation of SSMC) and Lighting was offset by declines at CE and Miscellaneous (due to Optical Storage seasonality and the NAVTEQ deconsolidation).

# Medical Systems

## Medical Systems: key data

in millions of euros unless otherwise stated

	Q3 2003	Q3 2004
Sales	1,413	1,408
Sales growth		
% nominal	(8)	0
% comparable	9	5
Income from operations	138	164
as a % of sales	9.8	11.6
Net operating capital (NOC)	4,607	3,815
Number of employees (FTEs)	30,826	30,856

## Business highlights

- The US Food and Drug Administration (FDA) approved the sale of the Philips Home HeartStart defibrillator to consumers without a prescription – the first and only of its kind to be cleared.
- Philips began global commercial shipments of its breakthrough Brilliance CT 40-channel system, upgradeable to 64-channel, the latter now available for orders. This 40-channel system advances routine clinical and diagnostic procedures, improving patient outcomes.
- Premier Purchasing Partners, LLP – a healthcare equipment purchaser affiliated with over 1,500 US hospitals – signed a 3-year agreement with Philips for the full line of medical imaging equipment and related services.

## Financial performance

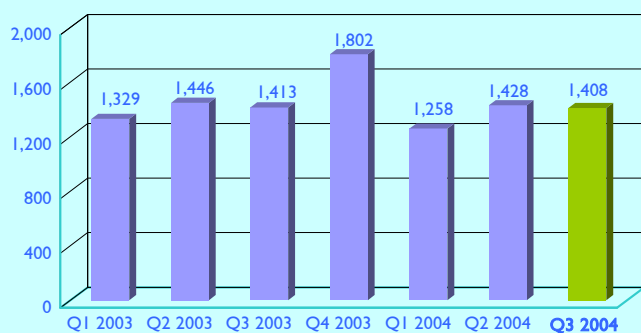
- Nominal sales were flat compared to 2003, while comparable sales grew 5%, mainly driven by Computed Tomography, Magnetic Resonance and X-Ray.
- Compared to last year, income from operations increased by EUR 26 million to EUR 164 million, thanks to higher sales volumes and improved margins in most businesses.
- All regions contributed to the comparable sales growth, in particular Latin America, Asia Pacific and EMEA.
- The order book remained strong. On a comparable basis, order intake increased by approximately 29%.

## Looking ahead

- With its continued strong order intake, Medical Systems is on track to reach 14% EBITA (12.2% income from operations) as a percentage of sales for 2004.

## Medical Systems sales

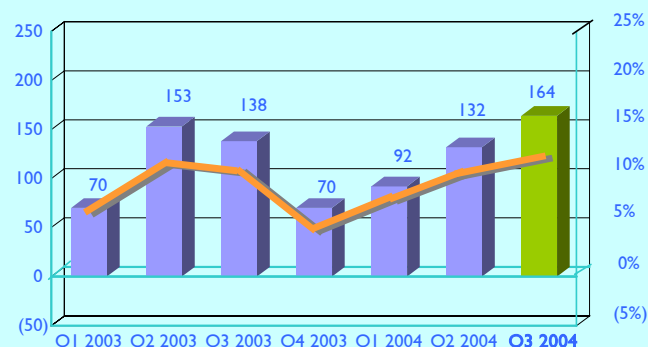
in millions of euros



## Medical Systems income from operations (IFO)

■ IFO in millions of euros

■ IFO as a % of sales



# Domestic Appliances and Personal Care (DAP)

## DAP: key data

in millions of euros unless otherwise stated

	Q3 2003	Q3 2004
Sales	466	450
Sales growth		
% nominal	(10 )	(3 )
% comparable	(3 )	0
Income from operations	82	82
as a % of sales	17.6	18.2
Net operating capital (NOC)	627	571
Number of employees (FTEs)	8,735	8,739

## Business highlights

- Philips and Procter & Gamble unveiled IntelliClean System from Sonicare and Crest – the first integrated power toothbrush and liquid toothpaste dispensing system.
- Philips and Interbrew announced a global partnership for PerfectDraft® – combining a high-quality appliance with consumer-preferred beer brands in light metal kegs.
- Philips announced the establishment of a new Consumer Health & Wellness Group to develop products and services that diagnose, monitor, improve and care for the health and wellbeing of consumers.

## Financial performance

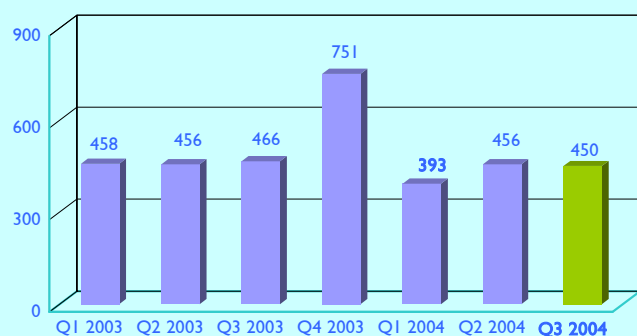
- Nominal sales declined by 3% compared to 2003. On a comparable basis sales were flat. Food & Beverage sales grew by 7%, mainly driven by the launch of the Senseo coffee maker in the USA. Shaving & Beauty sales remained flat, with lower sales in Western Europe and North America compensated by growth in China.
- Despite lower nominal sales, profitability rose to 18.2% on the back of strong margins across all businesses, which were primarily attributable to manufacturing efficiencies. Selling expenses rose slightly due to increased investments in advertising and promotion and in expanding retail channels.
- Continued focus on asset management led to a reduction in net operating capital compared to Q3 2003.

## Looking ahead

- The focus will remain on launching new products, extending partnerships and alliances, expanding retail channels into emerging markets and enhancing cost savings.
- Due to the traditionally high fourth-quarter sales, the bulk of the additional investments in advertising and promotion in the second half of 2004 will be concentrated in Q4.

## DAP sales

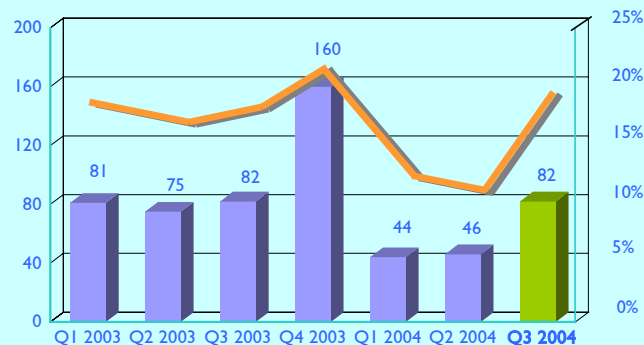
in millions of euros



## DAP income from operations (IFO)

IFO in millions of euros

IFO as a % of sales



# Consumer Electronics (CE)

## Consumer Electronics: key data

in millions of euros unless otherwise stated

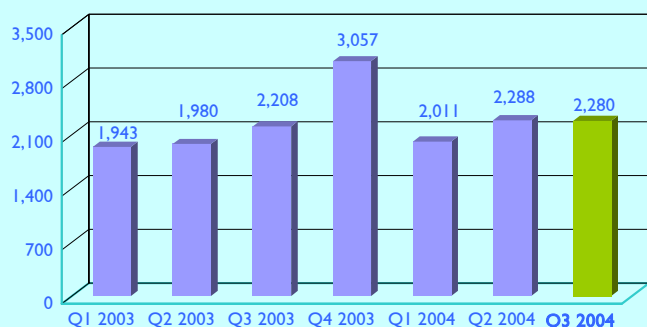
	Q3 2003	Q3 2004
Sales	2,208	2,280
Sales growth		
% nominal	(1)	3
% comparable	6	7
Income (loss) from operations	(32)	(15)
as a % of sales	(1.4)	(0.7)
Net operating capital (NOC)	150	308
Number of employees (FTEs)	19,893	18,996

## Business highlights

- The European Imaging & Sound Association (EISA) named the 37-inch FlatTV™ as “European LCD Television of the Year, 2004-2005” and the Streamium SL400i Wireless Multimedia Link as “European New Media: Video of the Year, 2004-2005”.
- In China, Philips began selling its full range of high-end home entertainment products – including the Ambilight TV and the DVD Recorder.
- Philips gained support from some 30 companies – including Apple, Nokia and Sony – for Advanced Video Coding (AVC), a new open compression standard for consumer digital video shown at the International Broadcast Conference 2004.

## Consumer Electronics sales

in millions of euros

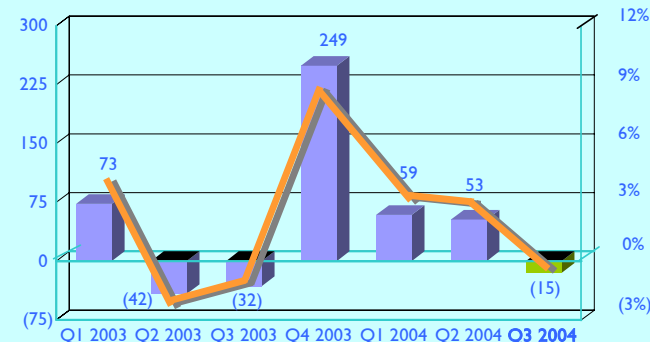


## Financial performance

- Comparable sales grew 7%, mainly driven by Connected Displays, Mobile Infotainment and Licenses.
- Income from operations improved by EUR 17 million due to license income of EUR 105 million (up from EUR 43 million last year) and cost savings generated by the Business Renewal Program. Income from operations was however severely impacted by a faster-than-expected decline in gross margins due to various factors including increased price competition, mainly in Europe, a sharp fall in panel prices and delayed product introductions in Mobile Infotainment.
- Income from operations included restructuring charges of EUR 27 million, approximately the same as last year.

## Consumer Electronics income from operations (IFO)

■ IFO in millions of euros      ■ IFO as a % of sales



## Looking ahead

- The Business Renewal Program is ahead of schedule to achieve EUR 400 million cost savings by year-end 2005.
- Restructuring charges of approximately EUR 70 million are expected in Q4 in connection with the Business Renewal Program and the reorganization of certain technology activities.
- Ongoing margin pressure is expected, especially in Europe.

## Lighting: key data

in millions of euros unless otherwise stated

	Q3 2003	Q3 2004
Sales	1,088	1,105
Sales growth		
% nominal	(4)	2
% comparable	2	7
Income from operations	124	142
as a % of sales	11.4	12.9
Net operating capital (NOC)	1,750	1,679
Number of employees (FTEs)	44,081	44,571

## Business highlights

- Philips became the first global car components supplier to ship mercury-free Xenon car lamps; these are installed in the Porte, one of Toyota's new green flagship vehicles.
- In Lisbon, Portugal, Philips provided all the lighting for the Luz Stadium, venue of the Euro 2004 soccer championship final.
- Philips launched the Mini Mastercolour for shop lighting applications. Small enough to be used in accent lighting for shop displays, this miniature ceramic discharge lamp is highly energy-efficient.

## Financial performance

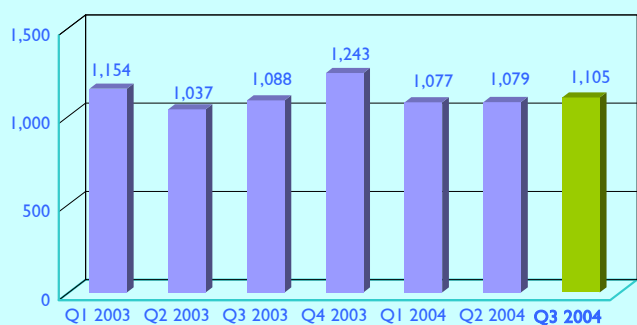
- All businesses except Luminaires gained market share.
- Compared to last year, sales increased by 2% on a nominal basis and 7% on a comparable basis, mainly driven by lamps in Europe and innovative UHP products.
- Income from operations increased by EUR 18 million compared to last year, fuelled by improved profitability in Lamps.
- At 12.9% of sales, income from operations reflected successful product innovation and cost management.

## Looking ahead

- Further optimization of supply chain management and ongoing strict cost control are planned.
- Increased investment in R&D and capital expenditures will continue to propel innovation.
- As part of the continued drive to optimize asset utilization, restructuring charges of approximately EUR 40 million are expected in Q4.

## Lighting sales

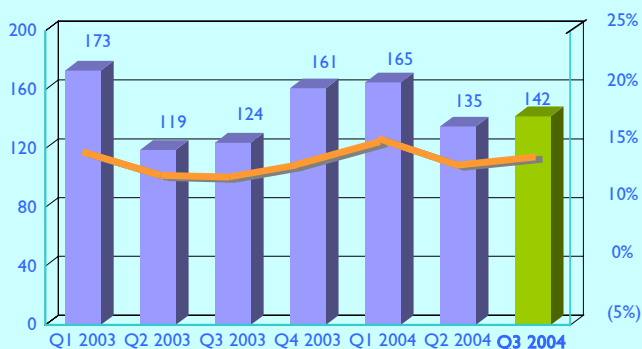
in millions of euros



## Lighting income from operations (IFO)

■ IFO in millions of euros

■ IFO as a % of sales



# Semiconductors

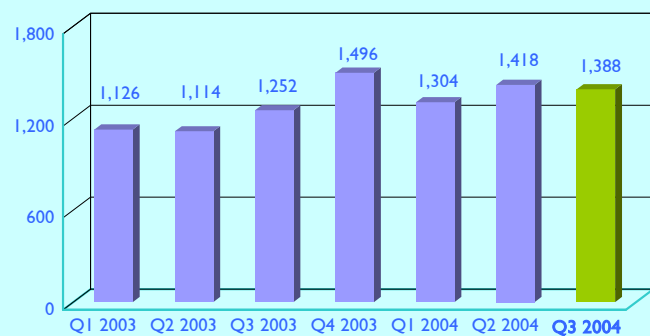
## Semiconductors: key data

in millions of euros unless otherwise stated

	Q3 2003	Q3 2004
Sales	1,252	1,388
Segment revenues	1,293	1,433
Segment revenues growth		
% nominal	(1)	11
% comparable	7	14
Income (loss) from operations	(191)	186
as a % of segment revenues	(14.8)	13.0
as a % of sales	(15.3)	13.4
Net operating capital (NOC)	2,899	3,254
Number of employees (FTEs)	33,843	35,925

## Semiconductors sales

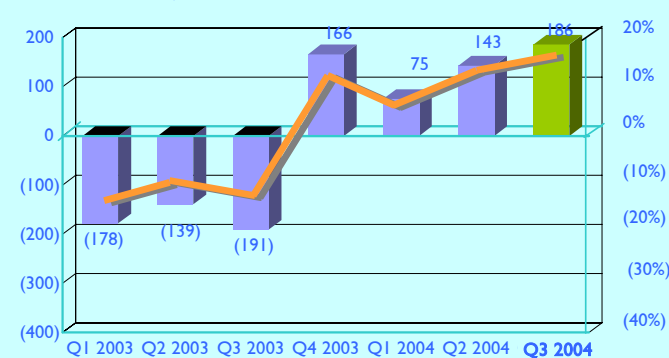
in millions of euros



## Semiconductors income from operations (IFO)

IFO in millions of euros

IFO as a % of sales



## Business highlights

- NASA selected Philips' advanced MIFARE® DESFire contactless chip technology to secure smart card access to its facilities.
- Samsung and Philips announced that they are to develop mobile devices based on Near Field Communication (NFC), enabling consumers to transfer pictures or data to NFC-enabled PCs or TVs from Samsung mobile devices equipped with Philips NFC chips.
- Philips announced its new Nexperia™ semiconductor reference design for DVD+RW video recorders, offering one of the industry's lowest system bill of materials.
- The Beijing Municipal Administration and Communications Card Co. Ltd. opted for Philips' MIFARE® UltraLight contactless chip technology in a new e-ticketing system for the Great Wall of China.

## Financial performance

- Segment revenues, excluding Mobile Display Systems (MDS), increased by 31% year-on-year and 2% compared with Q2 in US dollar terms. Sequential revenues of MDS declined by 10% in US dollar terms, reflecting a focus on higher margin products.
- The book-to-bill ratio declined from 1.13 at the end of Q2 to 0.66 at the end of Q3 due to shortening of the order book.
- Income from operations was again driven by the Standard Products and Mobile Communications businesses.
- Income from operations included a gain of EUR 51 million related to a property damage settlement for the fire in Caen (France) and EUR 10 million in respect of the related business interruption in the first half of the year. Restructuring charges in Europe totaled EUR 22 million, primarily for the reorganization of the fab in Nijmegen, The Netherlands.
- Last year, income from operations in Q3 was negatively impacted by restructuring and other charges totaling EUR 157 million.
- The utilization rate remained high at 98% (Q2: 99%).

## Looking ahead

- Sequential segment revenues are expected to be approximately flat in Q4 (in USD terms, excluding MDS). A double-digit sequential increase is forecasted for MDS (in USD terms).
- A lower utilization rate is expected due to a build-down of inventories in anticipation of Q1 sales.

# Miscellaneous

## Miscellaneous: key data

in millions of euros unless otherwise stated

	Q3 2003	Q3 2004
Sales	562	598
Sales growth		
% nominal	(20)	6
% comparable	(6)	17
IFO Technology Cluster	(79)	(84)
IFO Corp. Investments and others	(28)	657
Income (loss) from operations	(107)	573
as a % of sales	(19.0)	95.8
Net operating capital (NOC)	4	9
Number of employees (FTEs)	26,490	25,120

## Business highlights

- The initial public offering of NAVTEQ Corporation in August is seen as one of the most successful IPOs in the USA in 2004.
- Philips established an IP academy with two of China's most renowned universities – Renmin University and Tsinghua University, both of Beijing.
- At the High Tech Campus in Eindhoven, The Netherlands, Philips opened a world-class ElectroMagnetic & Cooling Competence Center for the design and testing of electromagnetic and thermal compatibility of equipment.
- For the third consecutive year, the World Intellectual Property Organization (WIPO) ranked Philips number 1 in patent filings.

## Financial performance Technology Cluster

- Results in the Technology Cluster were impacted by higher investments in development projects for new technologies.

## Financial performance Corp. Investments/others

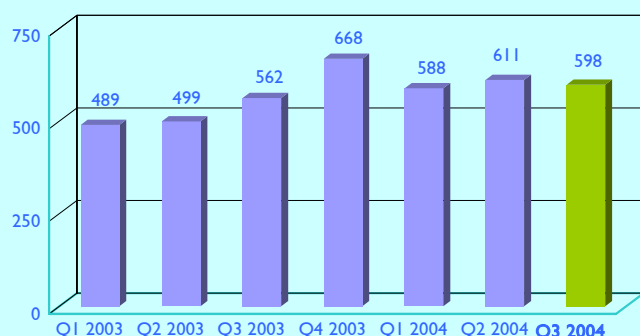
- The successful IPO of NAVTEQ resulted in a EUR 635 million gain on the sale of shares and a net cash inflow of EUR 672 million. Following the IPO, Philips' interest in NAVTEQ decreased from 83.5% to 34.8%.
- The increase in nominal sales was driven by Philips Enabling Technologies (ETG) and Optical Storage.
- ETG and Assembléon again showed an improvement in income from operations compared to last year. Optical Storage continued to perform strongly.
- We have received a settlement of EUR 20 million in respect of a portion of our asbestos product liability coverage. The company continued to accrue for loss contingencies based upon asserted claims and its settlement experience to date. The accrual in Q3 was higher than in Q2, and marginally higher than in Q1.

## Looking ahead

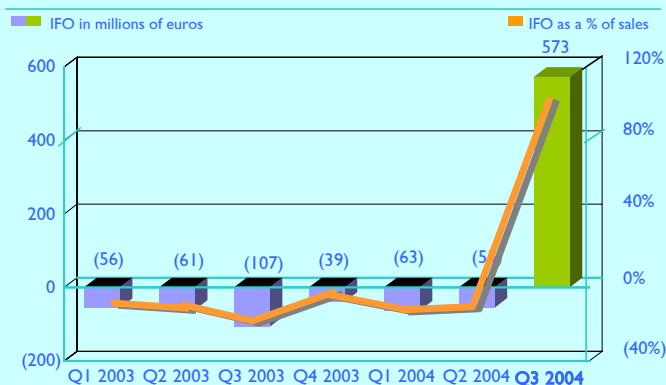
- Further execution of the divestment program is expected, assuming market conditions continue to improve.
- Restructuring charges of approximately EUR 65 million are expected in Q4 in connection with the reorganization of certain activities in the Technology Cluster.

## Miscellaneous sales

in millions of euros



## Miscellaneous income from operations (IFO)



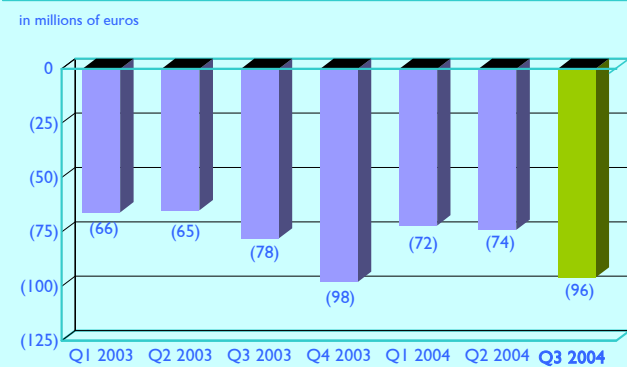
# Unallocated

## Unallocated: key data

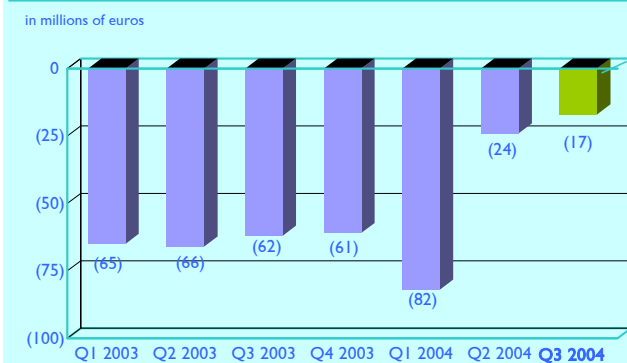
in millions of euros unless otherwise stated

	Q3 2003	Q3 2004
Corporate and regional overheads	(78 )	(96 )
Pensions	(62 )	(17 )
Income (loss) from operations	(140 )	(113 )
Number of employees (FTEs)	2,596	2,600

## Unallocated: Corporate and Regional Overheads income from operations (IFO)



## Unallocated: Pensions/postretirement benefit costs income from operations (IFO)



## Business highlights

- Philips announced its new brand promise, *sense and simplicity*, and introduced an innovative advertising campaign showing how the company delivers intuitive end-user experiences in Healthcare, Lifestyle and Technology.
- Philips was ranked number 1 on the Dow Jones Sustainability Index and was chosen by SustainableBusiness.com as one of the 20 companies comprising the 2004 SB20 list of the world's top sustainable stocks.
- In a survey carried out by Scenter, a leading Dutch management consultancy, Philips' 2003 Annual Report received the top score, described as "an outstanding demonstration of Philips' commitment to transparency and accountability".

## Financial performance

- Corporate and Regional Overhead costs were EUR 18 million higher than in Q3 2003, primarily due to the new brand campaign.
- Pension costs decreased by EUR 45 million compared to Q3 2003, mainly as a result of lower pension costs in The Netherlands.

## Looking ahead

- Compared to Q4 2003, costs related to Corporate and Regional Overheads are expected to be approximately EUR 25 million higher in Q4 2004 due to increased marketing investments and the roll-out of the new brand positioning.
- Income from operations related to pensions/postretirement benefit costs in the sector Unallocated in Q4 is forecasted at a loss of approximately EUR 30 million.

## LG.Philips Displays joint venture (100%)

in millions of euros unless otherwise stated

	Q3 2003	Q3 2004
Sales	861	830
Sales growth % nominal	(20 )	(4 )
Income from operations	9	56
as a % of sales	1.0	6.7
Net income (loss) (100%)	(32 )	40
Net income (loss) (Philips share = 50%)	(16 )	20
Net operating capital (NOC)	2,356	1,457
Number of employees (FTEs)	27,636	22,198

## LG.Philips Displays joint venture (100%)

- Q3 sales were driven by higher demand for both monitor and television tubes due to relatively high LCD panel prices.
- Income from operations improved from the last quarter, boosted by a EUR 13 million gain on the sale of land and buildings at the closed Newport site in Wales.
- Cash flow before financing activities was positive and showed a slight improvement compared to Q2.

## Looking ahead

- Restructuring will go on; restructuring and impairment charges of approximately EUR 70 million (Philips' share) are expected in Q4.

# Highlights in the 1<sup>st</sup> nine months

## The 1<sup>st</sup> nine months of 2004

- Net profit was EUR 2,338 million
- Nominal sales grew 6% – comparable sales up 10%, driven by Semiconductors and Consumer Electronics
- Income from operations was EUR 1,593 million
- Unconsolidated companies contributed EUR 1,224 million to net income
- Cash flow from operating activities was EUR 758 million
- Net debt : group equity ratio was 17 : 83

## Net income

in millions of euros

	Jan.- Sept. 2003	Jan.- Sept. 2004
Sales	20,020	21,140
Income (loss) from operations	(120 )	1,593
as a % of sales	(0.6 )	7.5
Financial income and expenses	(186 )	(201 )
Income taxes	113	(230 )
Results unconsolidated companies	323	1,224
Minority interests	(17 )	(48 )
Cumulative effect of change in accounting principle	(16 )	0
Net income	97	2,338
Per common share - basic	0.08	1.83
- diluted	0.08	1.82

## Group net income

### Net income

- Net income was a profit of EUR 2,338 million, compared to a net profit of EUR 97 million in the first nine months of 2003.
- Sales amounted to EUR 21,140 million, 6% higher than in the same period last year. The weaker US dollar and dollar-related currencies had a downward effect of 5%, while a 1% upwards effect was mainly due to the consolidation of SSMC in 2004 and the BenQ joint venture at Optical Storage in 2003.
- Comparable sales increased 10%, predominantly due to strong sales growth at Semiconductors (22%) and CE (12%). Sales growth at Medical Systems was 4%. Lighting was solid at 5%. At DAP, soft market conditions, in particular in Western Europe and North America, led to 2% lower sales.
- Income from operations was a profit of EUR 1,593 million, compared to a loss of EUR 120 million in the same period last year. Contributing to these improved results was a non-taxable gain on the IPO of NAVTEQ of EUR 635 million and an insurance settlement in respect of property and business interruption damage at Semiconductors. Restructuring and impairment charges totaled EUR 128 million, compared to EUR 400 million in the first nine months of last year. Pension costs amounted to EUR 218 million, compared to EUR 340 million in the same period last year.
- Unconsolidated companies contributed EUR 1,224 million to net income, compared to EUR 323 million in the first nine months of 2003. Contributing to these improved results were a dilution gain of EUR 156 million on Philips' participation in Atos Origin, a net gain of EUR 99 million related to InterTrust Technologies Corp. following its license agreement with Microsoft Corp., and a net gain of EUR 108 million related to the IPO of LG.Philips LCD. The latter company contributed EUR 561 million to net income, an increase of EUR 378 million.

### Other information

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Earlier we announced that MedQuist, in which Philips holds a stake of approximately 70.9%, had engaged outside counsel and an independent forensic accounting firm, to assist in investigations into allegations of potential improper billing practices. These investigations continued during the second quarter and a part of the third quarter. During the third quarter the law firm reported its findings to MedQuist's Board of Directors. However, based on this reporting it was not possible to draw any final conclusions about the financial impact, if any, for MedQuist. Therefore, the review of MedQuist's financial statements could not be completed in the third quarter and will continue during the 4th quarter. It remains uncertain when the review and the audit of the MedQuist financial statements can be completed.

As a consequence, Philips has not been able to complete its goodwill impairment test of the MedQuist investment.

A litigation claim by Volumetrics, Inc. is still pending. The oral arguments are scheduled for the end of October.

## Outlook

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Medical Systems is on track to achieve its target of 14% EBITA (12.2% income from operations) for 2004 based on strong orders for new products and cost control. In the seasonally strong fourth quarter, Domestic Appliances and Personal Care will capitalize on its innovations and market positions to achieve margins in the high teens. Lighting will continue to benefit from its investments in innovation and operational excellence, and will deliver another solid quarter. In Consumer Electronics, margins will recover somewhat as a result of seasonality, but will still be under pressure: this will lead to an acceleration of the Business Renewal Program and a furthering of ways to de-risk the business. Semiconductors will continue to benefit from design wins and asset-light manufacturing, while performing in line with or slightly better than the industry.

We expect 2004 to be one of Philips' better years.

Amsterdam, October 12, 2004

Board of Management

# Consolidated statements of income

all amounts in millions of euros unless otherwise stated

	2003	3 <sup>rd</sup> quarter 2004	January to September 2003	September 2004
Sales	6,989	7,229	20,020	21,140
Cost of sales	(4,854)	(4,817)	(13,613)	(14,097)
<b>Gross margin</b>	2,135	2,412	6,407	7,043
Selling expenses	(1,108)	(1,084)	(3,307)	(3,176)
General and administrative expenses	(348)	(326)	(1,092)	(1,018)
Research and development expenses	(609)	(641)	(1,892)	(1,909)
Impairment of goodwill	-	(4)	(9)	(18)
Restructuring and asset impairments	(208)	(58)	(391)	(110)
Other business income	12	720	164	781
<b>Income (loss) from operations</b>	(126)	1,019	(120)	1,593
Financial income and expenses	(24)	(70)	(186)	(201)
Income (loss) before taxes	(150)	949	(306)	1,392
Income tax (expense) benefit	54	(97)	113	(230)
Income (loss) after taxes	(96)	852	(193)	1,162
Results relating to unconsolidated companies including a year-to-date net dilution gain of EUR 221 million (2003: EUR 53 million)	239	337	323	1,224
Minority interests	(3)	(17)	(17)	(48)
Income before cumulative effect of a change in accounting principles	140	1,172	113	2,338
Cumulative effect of a change in accounting principles, net of tax	(16)	0	(16)	0
<b>Net income</b>	124	1,172	97	2,338
<b>Income (loss) from operations</b> as a % of sales	(1.8)	14.1	(0.6)	7.5
<b>Weighted average number of common shares</b> outstanding (after deduction of treasury stock) during the period (in thousands):				
• basic			1,276,791	1,280,091
• diluted			1,281,088	1,282,909
<b>Basic earnings per common share in euros:</b>				
Income before cumulative effect of a change in accounting principles	0.11	0.92	0.09	1.83
Net income	0.10	0.92	0.08	1.83
<b>Diluted earnings per common share in euros:</b>				
Income before cumulative effect of a change in accounting principles	0.11	0.91	0.09	1.82
Net income	0.10	0.91	0.08	1.82

The Group financial statements have been prepared on a basis consistent with US GAAP, which differs in certain respects from accounting principles as required by Dutch law (Dutch GAAP). Net income determined in accordance with Dutch GAAP amounted to a profit of EUR 2,028 million in the first nine months of 2004, compared to a loss of EUR 446 million in the corresponding period last year. These aggregate amounts result in basic earnings per common share of a profit of EUR 1.58 in January-September 2004, compared to a loss of EUR 0.35 last year. The difference between Dutch GAAP and US GAAP is caused by the fact that goodwill is no longer amortized under US GAAP and by income recognition in respect of reversals of security impairments under Dutch GAAP.

## Consolidated balance sheets and additional ratios

all amounts in millions of euros unless otherwise stated

### Consolidated balance sheet

	September 30, 2003	December 31, 2003	September 30, 2004
<b>Current assets:</b>			
Cash and cash equivalents	883	3,072	1,610
Receivables	5,072	4,628	5,215
Inventories	3,870	3,204	4,055
Other current assets	678	599	814
<b>Total current assets</b>	<b>10,503</b>	<b>11,503</b>	<b>11,694</b>
<b>Non-current assets:</b>			
Investments in unconsolidated companies	6,222	4,841	6,545
Other non-current financial assets	1,074	1,213	1,210
Non-current receivables	258	218	241
Other non-current assets	2,639	2,581	2,451
Property, plant and equipment	5,198	4,879	5,255
Intangible assets excluding goodwill	1,463	1,271	1,129
Goodwill	3,047	2,494	2,591
<b>Total assets</b>	<b>30,404</b>	<b>29,000</b>	<b>31,116</b>
<b>Current liabilities:</b>			
Accounts and notes payable	3,150	3,205	3,456
Accrued liabilities	3,495	2,754	3,188
Short-term provisions	939	949	918
Other current liabilities	687	649	717
Short-term debt	1,709	1,684	984
<b>Total current liabilities</b>	<b>9,980</b>	<b>9,241</b>	<b>9,263</b>
<b>Non-current liabilities:</b>			
Long-term debt	4,414	4,192	3,840
Long-term provisions	2,089	1,976	2,010
Other non-current liabilities	598	653	716
<b>Total liabilities</b>	<b>17,081</b>	<b>16,062</b>	<b>15,829</b>
Minority interests	167	175	315
Stockholders' equity	13,156	12,763	14,972
<b>Total liabilities and equity</b>	<b>30,404</b>	<b>29,000</b>	<b>31,116</b>
<b>Number of common shares outstanding</b>			
at the end of period (in thousands)	1,277,970	1,280,686	1,280,391
<b>Ratios</b>			
Stockholders' equity, per common share in euros	13,156 10.29	12,763 9.97	14,972 11.69
Inventories as a % of sales	13.4	11.0	13.4
Net debt : group equity ratio	28:72	18:82	17:83

Stockholders' equity determined in accordance with Dutch GAAP amounted to EUR 14,048 million as of September 30, 2004, compared to EUR 14,972 million under US GAAP.

The deviation is caused by the fact that goodwill under Dutch GAAP has to be amortized and charged to income, whereas under US GAAP it is no longer amortized, but instead tested for impairment.

## Consolidated statements of cash flows \*

all amounts in millions of euros

	2003	3 <sup>rd</sup> quarter 2004	January to September 2003	2004
<i>Cash flows from operating activities:</i>				
<b>Net income</b>	124	<b>1,172</b>	97	<b>2,338</b>
Adjustments to reconcile net income to net cash provided by operating activities:				
Depreciation and amortization	488	<b>411</b>	1,443	<b>1,207</b>
Impairment of equity investments	8	<b>0</b>	17	<b>4</b>
Net gain on sale of assets	(95)	<b>(660)</b>	(255)	<b>(705)</b>
Income from unconsolidated companies (net of dividends received)	(236)	<b>(265)</b>	(319)	<b>(1,142)</b>
Minority interests (net of dividends paid)	(4)	<b>11</b>	10	<b>35</b>
Decrease (increase) in working capital/other current assets	408	<b>(396)</b>	(391)	<b>(1,036)</b>
(Increase) decrease in non-current receivables/other assets	(285)	<b>(69)</b>	(227)	<b>35</b>
(Decrease) increase in provisions	(41)	<b>61</b>	(138)	<b>(13)</b>
Other items	9	<b>27</b>	82	<b>35</b>
<b>Net cash provided by operating activities</b>	376	<b>292</b>	319	<b>758</b>
<i>Cash flows from investing activities:</i>				
Purchase of intangible assets	(17)	<b>(26)</b>	(68)	<b>(56)</b>
Capital expenditures on property, plant and equipment	(264)	<b>(263)</b>	(661)	<b>(885)</b>
Proceeds from disposals of property, plant and equipment	23	<b>30</b>	114	<b>127</b>
Cash from derivatives	(28)	<b>56</b>	360	<b>93</b>
Proceeds from sale of other non-current financial assets	196	<b>0</b>	300	<b>6</b>
Proceeds from sale of businesses (purchase of businesses)	(76)	<b>367</b>	75	<b>309</b>
<b>Net cash (used for) provided by investing activities</b>	(166)	<b>164</b>	120	<b>(406)</b>
<b>Cash flows before financing activities</b>	210	<b>456</b>	439	<b>352</b>
<i>Cash flows from financing activities:</i>				
Decrease in debt	(823)	<b>(1,278)</b>	(879)	<b>(1,469)</b>
Treasury stock transactions	12	<b>7</b>	28	<b>(27)</b>
Dividends paid	-	<b>-</b>	(460)	<b>(460)</b>
<b>Net cash used for financing activities</b>	(811)	<b>(1,271)</b>	(1,311)	<b>(1,956)</b>
<b>Decrease in cash and cash equivalents</b>	(601)	<b>(815)</b>	(872)	<b>(1,604)</b>
Effect of change in consolidations on cash positions	-	<b>-</b>	-	<b>117</b>
Effect of changes in exchange rates on cash positions	(9)	<b>(9)</b>	(103)	<b>25</b>
Cash and cash equivalents at beginning of the period	1,493	<b>2,434</b>	1,858	<b>3,072</b>
<b>Cash and cash equivalents at end of period</b>	883	<b>1,610</b>	883	<b>1,610</b>

\* For a number of reasons, principally the effects of translation differences and consolidation changes, certain items in the statements of cash flows do not correspond to the differences between the balance sheet amounts for the respective items.

## Consolidated statement of changes in stockholders' equity

all amounts in millions of euros

	January to September 2004								
	Common stock	Capital in excess of par value	Retained earnings	Accumulated other comprehensive income (loss)			Treasury shares at cost	Total stock- holders' equity	
				Translation differences	Available for sale securities	Minimum pension liability			Cash flow hedges
Balance as of December 31, 2003	263	71	16,970	(3,364)	416	(362)	25	(1,256)	12,763
Net income			2,338						2,338
Net current period change				287	18	(7)	(30)		268
Reclassifications into income				38			14		52
<b>Total comprehensive income (loss), net of tax</b>			2,338	325	18	(7)	(16)		2,658
Dividend payable			(460)						(460)
Purchase of treasury stock								(96)	(96)
Re-issuance of treasury stock		(10)						86	76
Stock options: compensation plans		31							31
<b>Balance as of September 30, 2004</b>	<b>263</b>	<b>92</b>	<b>18,848</b>	<b>(3,039)</b>	<b>434</b>	<b>(369)</b>	<b>9</b>	<b>(1,266)</b>	<b>14,972</b>

## Product sectors

all amounts in millions of euros unless otherwise stated

### Segment revenues and income from operations

	3 <sup>rd</sup> quarter					
	2003			2004		
	segment revenues	Income (loss) from operations		segment revenues	Income (loss) from operations	
	amount	as a % of segment revenues		amount	as a % of segment revenues	
Medical Systems	1,416	138	9.7	<b>1,410</b>	<b>164</b>	<b>11.6</b>
DAP	471	82	17.4	<b>454</b>	<b>82</b>	<b>18.1</b>
Consumer Electronics	2,228	(32)	(1.4)	<b>2,303</b>	<b>(15)</b>	<b>(0.7)</b>
Lighting	1,094	124	11.3	<b>1,113</b>	<b>142</b>	<b>12.8</b>
Semiconductors	1,293	(191)	(14.8)	<b>1,433</b>	<b>186</b>	<b>13.0</b>
Miscellaneous	765	(107)	(14.0)	<b>820</b>	<b>573</b>	<b>69.9</b>
Unallocated		(140)			<b>(113)</b>	
Total	7,267	(126)		<b>7,533</b>	<b>1,019</b>	
Intersegment revenues	(278)			<b>(304)</b>		
<b>Sales</b>	6,989			<b>7,229</b>		
<b>Income (loss) from operations as a % of sales</b>		(1.8)			<b>14.1</b>	

## Product sectors (continued)

all amounts in millions of euros unless otherwise stated

### Segment revenues and income from operations

	January to September					
	2003			2004		
	segment revenues	Income (loss) from operations		segment revenues	Income (loss) from operations	
	amount	as a % of segment revenues		amount	as a % of segment revenues	
Medical Systems	4,198	361	8.6	4,105	388	9.5
DAP	1,393	238	17.1	1,310	172	13.1
Consumer Electronics	6,189	(1)	-	6,640	97	1.5
Lighting	3,296	416	12.6	3,284	442	13.5
Semiconductors	3,621	(508)	(14.0)	4,242	404	9.5
Miscellaneous	2,152	(224)	(10.4)	2,434	455	18.7
Unallocated		(402)			(365)	
Total	20,849	(120)		22,015	1,593	
Intersegment revenues	(829)			(875)		
<b>Sales</b>	20,020			21,140		
<b>Income (loss) from operations as a % of sales</b>		(0.6)			7.5	

## Product sectors, main countries and regions

all amounts in millions of euros

### Sales and total assets

	<b>Sales (to third parties)</b>		<b>Total assets</b>	
	January to September		September 30,	
	2003	2004	2003	2004
Medical Systems	4,188	4,094	6,360	5,685
DAP	1,380	1,299	1,037	962
Consumer Electronics	6,131	6,579	2,775	2,856
Lighting	3,279	3,261	2,605	2,598
Semiconductors	3,492	4,110	6,341	4,745
Miscellaneous	1,550	1,797	5,673	8,051
Unallocated			5,613	6,219
<b>Total</b>	20,020	21,140	30,404	31,116

### Sales and long-lived assets

	<b>Sales (to third parties)</b>		<b>Long-lived assets *</b>	
	January to September		September 30,	
	2003	2004	2003	2004
Netherlands	811	814	1,616	1,524
United States	5,403	5,037	4,755	3,864
Germany	1,523	1,656	630	592
France	1,293	1,312	220	191
United Kingdom	819	825	267	220
China	1,913	2,185	365	432
Other countries	8,258	9,311	1,855	2,152
<b>Total</b>	20,020	21,140	9,708	8,975

\* Includes property, plant and equipment and intangible assets.

### Sales by region

	<b>Sales (to third parties)</b>	
	January to September	
	2003	2004
Europe/Africa	8,605	8,987
North America	5,660	5,312
Latin America	837	1,035
Asia Pacific	4,918	5,806
<b>Total</b>	20,020	21,140

## Pension costs

all amounts in millions of euros unless otherwise stated

In accordance with SFAS No. 132 (revised 2003) the components of net periodic pension costs and costs of postretirement benefits other than pensions are the following:

### Net periodic pension costs of defined-benefit plans

	3 <sup>rd</sup> quarter 2004		January-September 2004	
	Netherlands	Other	Netherlands	Other
Service cost	39	26	130	83
Interest cost on the projected benefit obligation	145	96	450	285
Expected return on plan assets	(179)	(91)	(542)	(272)
Net amortization of unrecognized net transition (assets)/liabilities	-	1	-	9
Net actuarial (gain) loss recognized	-	(3)	(2)	13
Amortization of prior service cost	(14)	7	(28)	20
Settlement loss	-	1	34	2
Other	(4)	1	(8)	3
<b>Net periodic cost (income)</b>	<b>(13)</b>	<b>38</b>	<b>34</b>	<b>143</b>

The net periodic pension costs in the third quarter of 2004 amounted to EUR 41 million, of which EUR 25 million for defined-benefit plans (the Netherlands EUR (13) million, Other countries EUR 38 million) and EUR 16 million related to defined-contribution plans outside the Netherlands.

### Net periodic costs of postretirement benefits other than pensions

	3 <sup>rd</sup> quarter 2004		January-September 2004	
	Netherlands	Other	Netherlands	Other
Service cost	3	1	9	3
Interest cost on the accumulated postretirement benefit obligation	5	6	14	18
Amortization of unrecognized transition obligation	1	1	3	4
Net actuarial loss recognized	1	-	4	3
Curtailment loss	-	-	-	2
<b>Net periodic cost</b>	<b>10</b>	<b>8</b>	<b>30</b>	<b>30</b>

## Philips quarterly statistics

all amounts in millions of euros unless otherwise stated; percentage increases always in relation to the corresponding period of the previous year

	2003				2004			
	1 <sup>st</sup> quarter	2 <sup>nd</sup> quarter	3 <sup>rd</sup> quarter	4 <sup>th</sup> quarter	1 <sup>st</sup> quarter	2 <sup>nd</sup> quarter	3 <sup>rd</sup> quarter	4 <sup>th</sup> quarter
Sales	6,499	6,532	6,989	9,017	6,631	7,280	7,229	
% increase	(14)	(18)	(4)	1	2	11	3	
Income (loss) from operations	32	(26)	(126)	608	218	356	1,019	
as a % of sales	0.5	(0.4)	(1.8)	6.7	3.3	4.9	14.1	
% increase	(56)	.	.	.	.	.	.	
Net income (loss)	(69)	42	124	598	550	616	1,172	
% increase	.	.	.	.	.	.	.	
per common share in euros	(0.05)	0.03	0.10	0.46	0.43	0.48	0.92	
	January- March	January- June	January- September	January- December	January- March	January- June	January- September	January- December
Sales	6,499	13,031	20,020	29,037	6,631	13,911	21,140	
% increase	(14)	(16)	(13)	(9)	2	7	6	
Income (loss) from operations	32	6	(120)	488	218	574	1,593	
as a % of sales	0.5	0.0	(0.6)	1.7	3.3	4.1	7.5	
% increase	(56)	.	.	16	.	.	.	
Net income (loss)	(69)	(27)	97	695	550	1,166	2,338	
% increase	.	.	.	.	.	.	.	
as a % of stockholders' equity (ROE)	(2.1)	(0.3)	1.0	5.3	18.5	19.0	24.5	
per common share in euros	(0.05)	(0.02)	0.08	0.54	0.43	0.91	1.83	
	period ending 2003				period ending 2004			
Inventories as a % of sales	12.1	12.8	13.4	11.0	12.1	12.5	13.4	
Net debt : group equity ratio	30:70	29:71	28:72	18:82	18:82	21:79	17:83	
Total employees (in thousands)	166	164	166	164	165	166	167	

Information also available on Internet, address: [www.investor.philips.com](http://www.investor.philips.com)

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