



## Conference Call Transcript

PHG - Q1 2006 Royal Philips Electronics Earnings Conference Call

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*Deutsche Bank - Analyst*

**Matthew Gehl**

*Goldman Sachs - Analyst*

**Jonathan Dutton**

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## PRESENTATION

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### Operator

Welcome to the Royal Philips Electronics First Quarter Results call on Tuesday April 18, 2006. During the introduction by Mr. Pierre-Jean Sivignon all participants will be in a listen only mode. After the presentation there will be an opportunity to ask questions. [OPERATOR INSTRUCTIONS].

I will now hand the conference over to Mr. Pierre-Jean Sivignon. Please go ahead sir.

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### Pierre-Jean Sivignon - *Royal Philips Electronics - CFO*

Thank you. Ladies and gentlemen, let me firstly welcome you to this conference call for the first quarter results of 2006 for Royal Philips Electronics. I will make a few introductory remarks and then open up the call to your questions.

This quarter has again been the one in which we have seen more evidence that the targets we have set for ourselves are being, or will be, met. Let me be more specific. The comparable growth for the company was 10%, with all main divisions contributing towards this figure. In fact, the

lowest for any division was 8% growth. The growth in the quarter supports our average annual target of 5 to 6% growth on comparable terms, and I mean organic growth.

The EBIT margin in the quarter was 4.5% compared to 3.2% in 2005. This improvement quarter-over-quarter helps us move towards our target of 7 to 10% as from the end of 2006. Please remember that the fourth quarter is always our strongest quarter.

In Medical Systems the comparable growth was 8%, which supports our annual target of 6%. This was also underpinned by the 18% growth in equipment order intake, which is a continuation of the strong trend that we saw last year. In addition, the order intake for Medical IT was excellent.

The margin continues to be affected by the same factors that we saw in the fourth quarter of 2005, however this in no way diminishes our expectation to return to higher margins within a few quarters as we have identified the actions to be taken and these are in process.

In DAP, the excellent quarter has given us a 10% comparable growth which supports our target of 7% for the year. As part of this high growth rate we saw continuation of the success of our new shaving range. The underlying developments of the margin were strong and supports our annual target of 15 to 16%. We continue to work towards taking costs out of this division.

The growth rate in Consumer Electronics was very high at 16% which reflects the continuing move to flat screen television, and to a smaller extent our growth in peripherals and accessories. The margin in the quarter again shows that we are on track to repeat the 4 to 4.5% target.

The Lighting sales now; the Lighting sales growth was 8%. That was fairly widely spread on a product and geographic basis, and supports our annual target of 6%. The comparable sales growth of Lumileds was 25% which is in line with our expectations at the time of the acquisition. The Lighting margin was good and we continue to take costs out of this division.

The Semiconductors sales showed a comparable growth of 13%, and the sequential decline was in line with our expectations. The published margin was 7.3%, but excluding a restructuring charge and costs related to the legal separation, the margin was 9%. We are very pleased with the developments taking place in this division, based on the business renewal program. The separation of the Semiconductor activities into a separate legal structure are progressing well and are on track to be completed by the end of the third quarter.

As you can understand, I cannot say anything about any ongoing discussions of a strategic nature which have a maximum value creation focus. However, we are continuing with the appropriate speed and at the time our options remain open.

In Other Activities, we have announced the disposal of some businesses during the quarter, and we are making progress with others. I expect that we will make further announcements soon.

The average quarterly run rate for EBIT for this sector for this year should be similar to the amount in the first quarter of 2006. The EUR800 million net cash at the beginning of the quarter turned into a net debt of EUR1.3 billion at the end of the particular quarter, and this was principally due to items that we already told you about. These were the payments for Lifeline, the funding of the UK pension fund and the completion of the share buyback program.

We are not announcing another buyback program at this moment in time for principally two reasons. Firstly it will take another two months to complete the legal steps to cancel the shares from our completed buybacks, and secondly we need to finalize our view on the potential for acquisitions.

The inventory percentage of 12.3% is marginally higher than one year ago; I recall it was at 12%. There are still one or two areas where the inventory to sales ratio can be improved which we are working on.

The results from non-consolidated companies include 45 million for the voluntary support of social plans for employees impacted by the bankruptcy of some LG Philips display activities. The main item in this part of our results is that from LG LCD as TSMC is now accounted for on a dividend basis which will be included in the second quarter.

Let me now open the call for your questions.

## QUESTION AND ANSWER

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**Operator**

Thank you sir. [OPERATOR INSTRUCTIONS]. Would you please limit yourselves to one question with a maximum of one follow-up. This will give more people the opportunity to ask questions. [OPERATOR INSTRUCTIONS]. There will be a short pause while participants register for a question. The first question comes from Mr. Nav Sheera. Please state your company name followed by your question.

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**Nav Sheera - Lehman Brothers - Analyst**

Good morning. Nav Sheera from Lehman Brothers. Pierre-Jean, I just wanted to ask you some more detail about what you are doing in terms of the Medical Systems margins, because I've seen obviously from last quarter that it was [consummate late] in orders due to new products, and some of the emerging market activities. What specifically are you doing that you believe that will lead to better margins for the next few quarters?

And I've got one follow-up on Semis. Thank you.

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**Pierre-Jean Sivignon - Royal Philips Electronics - CFO**

Right. Well I think Medical -- the margin of Medical, if you actually strip it of exceptionals is actually in absolute terms in line with last year, in absolute euros. Basically, this particular quarter still I think the gross margin we need to improve, and there we told you what we were doing at the end of Q4, and we are consistently pursuing that, which is if you remember low cost sourcing, low cost manufacturing; I think those elements are very much still in play.

The other thing which is very much in play is obviously the improvement of the mix. To prepare for this call I actually looked at, in details, in the mix between service and products by geographic areas, and today, given the very strong growth of our equipment sales and of our install base, that growth of equipment is still in a number of regions outpacing the growth of the service business. In other words, our increase of revenue coming from equipment sales, as we speak, is still going faster than service.

And of course that has an impact on the mix, and the time will come where obviously this will go the other way round and the better margin on services will start to help us. But today the only territory where this is the case, i.e. where the growth of service is actually higher than the growth of equipment, that's actually the US, which is the most mature of our territories. In the other territories, that's not the case today.

So one of the other elements if you remember of Q4 was that the mix between service and equipment sales, which obviously we want to push more towards service, and as equipment sales are growing quite rapidly, we have that mismatch right now. So that's the second element.

In terms of reorganizing, we've disclosed to you that we've made a few moves in the US; actually it is in our press release that we are combining the manufacturing for Nuc Med, and we've moved it from California to actually Cleveland, I think, and we've actually combined the two sites that we have there, so we are doing that as well.

And last, but not least, I will say that in the first quarter of '06, our selling expenses were a bit high, and that was on the back of the reorganization of the selling structure, selling and service structure, that we have now centralized with centralized management, and we have some one-off costs in this particular quarter on the back of that.

So those four things together would be my answer to your question.

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**Nav Sheera - Lehman Brothers - Analyst**

Thank you for the comprehensive answer. And just one thing on Semis; I notice that your book-to-bill ratio was 1.12 which is a lot higher than last quarter. Is this across all end markets or is there something specific, e.g. wireless, which is driving the increased order activity? Thank you.

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**Pierre-Jean Sivignon - Royal Philips Electronics - CFO**

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Well, I think the activity while strong, well actually, to be totally clear, was actually stronger than we thought. It was true across our four verticals. Now if I had to pick up two verticals which have done better, that would be multi-market, but certainly as well automotive and identification. I mean, those are the two where I think we've been doing better. But all in all, I would say a strong quarter everywhere, and ahead I think of what you guys were expecting, and certainly ahead of -- probably a bit ahead as well of our own expectations.

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**Operator**

Thank you. The next question comes from Mr. Nicolas Gaudois. Please state your company name followed by your question.

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**Nicolas Gaudois - Deutsche Bank - Analyst**

Yes, hello, Nicolas Gaudois from Deutsche Bank. I've got a first question, Pierre-Jean, on Medical, and then a follow-up if I may on the Consumer side. On Medical, could you give us some generality on IT and software revenues. I think you indicated in the press release that the start of the year was strong. Could you get us more details on what is the strength coming from your iSite launch as well as on the Epic side, Xtenity? And how do you expect these to potentially help margins as well within the next 12 to 24 months?

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**Pierre-Jean Sivignon - Royal Philips Electronics - CFO**

Okay. I think the -- you have to realize I am absolutely prepared to talk about that, but you have to realize that in relative terms compared to the rest, it is still very small. But to give you an idea on Medical IT, the growth for Q1 '06 compared to Q1 '05 was a bit north of 20%, so that tells you that the growth there, and I'm talking about revenue growth, is north of what we see on the rest of the activity. But that's -- in relative terms that is small. Today it is I would say below 10%. I can't be much more specific, but keep in mind that it's below 10%. So it's still a small amount in absolute terms, but good growth in relative terms.

In terms of bottom line, it's hard basically to be too specific now, because we are still in the integration phase of Stentor. We basically are seeing incoming orders on their own products -- on their own patch product, which is clearly ahead of what we had expected. I think we disclosed in the press release some numbers there, so that's clearly going faster than we thought. In terms of contribution to the bottom line, we will have to wait for a couple of quarters, because the business model -- the nature of the business model of Stentor, is going to make that it will be a sustainable line, because as you know it's a pay-per-use, so it's going to be more sustainable than in the previous model we had with the Philips product, but it's only going to take probably -- it's only going to come in the latter part of '06 if not in '07. So basically, the bottom line impact from Stentor, net net, is still to come, after a couple of quarters of integration coming from the new business model of Stentor compared to what we had before. But if anything, the news there is going to be better than what we had anticipated when we acquired the company.

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**Nicolas Gaudois - Deutsche Bank - Analyst**

Great. And actually my follow-up is on Semis, not Consumer. Could we have a progress report please on your cost-cutting program, EUR250 million per annum by '07 you announced in September? How much do you think of that is already completed? And also could you qualify this qualitatively?

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**Pierre-Jean Sivignon - Royal Philips Electronics - CFO**

Yes, it's hard obviously to be totally specific. The one territory I can be specific on; on the depreciation side I would say there I think I can give you the guidance that you probably don't have yet. I would say that probably the reduction of depreciation would be around 100 million, I think, on the back of '06. So by the end of '06 you should see that 100 million come off our depreciation line as part of that business renewal plan. I think for the rest of the plan, which are all the other elements, it's going along. I think it's probably going I would say in due proportion to the time which has lapsed. If I can give you a guidance, in terms of impact on the bottom line, I would say that that plan started last year. We gave ourselves a period of time of two years, by the end -- we said this plan would be completed by the end of '07, and I would say the progress is probably going along as a proportion of the time which has lapsed on the non-depreciation part of that plan. So I would say I'll let you run the math there.

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**Nicolas Gaudois - Deutsche Bank - Analyst**

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Okay, that's great. Thank you.

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**Pierre-Jean Sivignon - Royal Philips Electronics - CFO**

But it's on plan. Nicolas, the thing is, obviously it's not exactly the way we had planned it a year ago, but in terms of progress and in terms of impact I think we will be on target.

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**Nicolas Gaudois - Deutsche Bank - Analyst**

Okay, thank you Pierre-Jean.

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**Operator**

Thank you. The next question comes from Mr. Matthew Gehl. Please state your company name followed by your question.

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**Matthew Gehl - Goldman Sachs - Analyst**

Yes, with Goldman Sachs. Just wanted to follow-up on the questions on Medical, and hoping to just get a bit more detail on the Q2 environment. With these costs you mentioned in Q1, just interested in how much of an impact they'll still have in Q2 and wondering if you could just make a comment? You said, excluding MedQuist your absolute margin in Q1 was higher than it was in Q1 of 2005. Do you think that's a trend that can remain constant in Q2, i.e. is your Q2 absolute margin going to be above what it was in 2005?

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**Pierre-Jean Sivignon - Royal Philips Electronics - CFO**

Right. I think yes, indeed, I said excluding MedQuist the absolute margin was at level, absolutely.

As far as Q2 is -- I mean the guidance we have given to you for the whole year was that the margin of '06 will be higher than the margin of '05. That guidance we have given to you and we stand by it. Now we start Q1 with a margin which is in percentage terms lower than the one of '05, so it means that gradually we are guiding you for a gradual bounce back. I think there is nothing new compared to what we said in January. We said that we would have a slower start of the year at Medical in line with Q4 of last year, and we would have a stronger second part of the year. So all that guidance absolutely stands, and Q2 will probably stand in the middle. So I would say if I were to guide you on Q2, that would be something between a lower Q1 as we have seen it now, and of course a stronger second half, so that would be some time -- something in between those two borders for the margin of the second quarter.

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**Matthew Gehl - Goldman Sachs - Analyst**

So you're saying -- you didn't say below Q1, you said --

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**Pierre-Jean Sivignon - Royal Philips Electronics - CFO**

No, I said for Q1 was lower in percentage than last year and I'm saying that still in percentage or Q2 should be in line with last year, even that we plan to add the overall year up and accordingly obviously the second half of the year clearly stronger. So I said that Q2 should be in percentage between what we've seen in Q1 and what we expect for the second half. And I'm talking percentage margin.

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**Matthew Gehl - Goldman Sachs - Analyst**

Okay so somewhere between around the 7% level and RPM where you second half target is?

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**Pierre-Jean Sivignon - Royal Philips Electronics - CFO**

Right.

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**Matthew Gehl - Goldman Sachs - Analyst**

Okay. And a follow-up on the Semiconductor business. Can you give us a sense of what happened with the inventory levels in the Semiconductor business both for yourself, and if you have any comment on what you're seeing with your distribution partners that would be extremely helpful?

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**Pierre-Jean Sivignon - Royal Philips Electronics - CFO**

Well actually the inventory for -- I mean I think we are in the same situation at the end of Q1 as we were at the end of the fourth quarter which is to say that in the inventory channels we don't see any real piling up of inventory. Actually basically we made the point at the end of the fourth quarter where we said the channels looks okay to us, nothing particular to report, no old products in the pipeline. And in percentage terms, actually I could tell you that the end of the first quarter '06 is in line with the fourth quarter '04. I could go as far as telling you that expressed in percentage the inventory has actually come down a little bit from the level it was at the end of the previous quarter. So I would say a situation which is quite comparable to the one we had at the end of the previous quarter.

I can't really comment on the industry; you guys probably have spent more time than I have on this, but it looks like we are very much in the same situation that we were at the end of Q4.

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**Matthew Gehl - Goldman Sachs - Analyst**

Great, thank you.

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**Operator**

Thank you, the next question comes from Mr. Jonathan Dutton. Please state your company name followed by you question.

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**Jonathan Dutton - UBS - Analyst**

Yes good morning, it's from UBS. Just a couple of questions, firstly on Semis. On a year-on-year basis the margins have improved from 1 to 9% and I think in the past you've guided to a 5 to 15% margin target. Do you think that's something of a conservative assumption based on the margin improvement that you're pushing through? And also could you possibly just elaborate a bit on how much of a contribution Nexperia is making to the margin expansion and the sales in 2006?

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**Pierre-Jean Sivignon - Royal Philips Electronics - CFO**

Okay, I think the guidance we gave to you was indeed 5 minimum, 15 max. That was the band width we had given, but we -- if you read what we mentioned at the time, I think when we refer to the 15% we mention a minimum of 15% in the upper part of the cycle. So that turnover you are referring to is a turnover which is giving you a min and a max, but we presented the max at the time as something which would be the minimum in the upper part of the cycle.

Now if -- I mean, are the results of first quarter which are all clear of exceptionals because you've seen in the press release that we had actually two exceptionals in the first quarter. We had one restructuring for the selling organization in Europe and we had the legal cost for the carve out of the division. And if you exclude those elements the margin indeed stood at almost -- actually 9% for the first quarter. Does that make us change the guidance? No, I think clearly it gives us comfort. Clearly those numbers are north of what we were expecting, but I don't think we want to guide you anywhere different that what we've done it so far. But my only body language there is certainly that this first quarter was a bit stronger than we thought yes, but not in terms of guidance, no change.

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**Jonathan Dutton - UBS - Analyst**

Great, I've just got one quick follow-up on the Consumer Electronics business. The top line growth was the strongest on a divisional basis, I just wondered if you could share your views on the outlook for the LCD TV market, what the level of inventories are and what sort of sales growth we might look for in the next few quarters ahead of the World Cup?

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**Pierre-Jean Sivignon - Royal Philips Electronics - CFO**

Right, just before I go to this, you ask about Nexperia, I'm sorry, just a word on Nexperia. Nexperia is absolutely fundamental to the growth on the TV side and clearly obviously I would say at the centre stage on the digital side of the television for that particular vertical. So certainly Nexperia as in the previous couple of quarters quite crucial to our growth there.

To your question now on LCD; no I'm not aware of high inventory in LCD, if anything on LCD, very, very good growth. Is it going to increase even more on the back of the World Cup? Hard to say. I think we -- the World Cup is very important indeed for us in terms of event, but as you know we have one event like this every year. I would say for us the World Cup is probably important from another angle, it will be the first time that high definition signal will be broadcast [native] for a major world sport event. And I would like to say that probably in terms of viewing experience, if anything that's more important for us than the World Cup per se.

In terms of impact on the margin, as you know we have structured the business model of Consumer Electronics to be somewhat independent from the volumes, right? So to answer your question, yes we could see more volumes in Q2 on the back of that, but the importance for us is the confirmation that our business model is rock solid regardless I would say of the fluctuations during the year to deliver to you the 4 to 4.5%.

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**Jonathan Dutton - UBS - Analyst**

Great, thanks very much.

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**Operator**

Thank you. The next question comes from Mr. Janardan Menon. Please state your company name followed by your question.

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**Janardan Menon - Dresdner Kleinwort Wasserstein - Analyst**

Hi it's Janardan from Dresdner Kleinwort Wasserstein. Just a question on Lighting; you've done extremely well on Lighting in the quarter, I was just wondering how much of that is from Lumileds and how much are other factors? And more importantly, how sustainable is it through the rest of the year and future years? What I'm asking is, are we taking this to a sort of higher level altogether on Lighting because of certain factors or is there some one-off factors in Q1 right now?

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**Pierre-Jean Sivignon - Royal Philips Electronics - CFO**

Okay, I think as far as the Lighting is concerned, I'm glad you mention it because indeed actually Lighting came up quite strong. I think 8% growth year-on-year, clean growth, comparable, I think you will agree with me that's a pretty strong number and that is certainly on the back of all the money invested in engineering in the last couple of years, so strong growth.

Now to your question on Lumileds; when we acquired Lumileds if you remember last year when we disclosed the announcement on Lumileds mid-August, we talked about two numbers. We talked about a growth of 25% revenue and we talked as well about the guidance of EBITDA 25%. What we see in this first quarter on Lumileds are exactly those numbers. Indeed a growth of 25%, so strong growth, very much in line with what we have guided you on. And the other thing as well was the EBITDA margin of 25%, very much present there as well.

So Lumileds is indeed adding an impact on Lighting, but please exclude Lumileds when you do your math, work backward and you will see that the performance of Lighting is not only Lumileds. You will see that basically Lighting has grown in about all its verticals and the other interesting thing is that, in terms of regions, the growth of Lighting was actually quite evenly spread. So I think it's, all in all, a pretty strong quarter, even if you exclude the couple of exceptionals which we have disclosed in the press release. But certainly Lumileds help here and on the way to continue to help. Definitely in line with the guidance we gave at the acquisition time.

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**Janardan Menon - Dresdner Kleinwort Wasserstein - Analyst**

And you've said you're going to deconsolidate Philips BenQ optical storage for about EUR650 million of revenue. Can we assume that that is a breakeven business and therefore will make no impact on your absolute profits, but will increase the margin of the company?

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**Pierre-Jean Sivignon - Royal Philips Electronics - CFO**

You can make that assumption. By the way the 650 million is on a 12 year -- sorry a 12 months basis. Of course on three quarters you will have to take the proportion, but your assumption is correct.

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**Janardan Menon - Dresdner Kleinwort Wasserstein - Analyst**

And just a last question is on Consumer Electronics. You may defer from me I think, but you've got very, very strong sales with your sales rising almost EUR300 million plus, year-on-year. But your margin doesn't seem to have shown that much of leverage in the course of the quarter. Am I reading that wrong or was there some kind of price pressure or any negative factors in the quarter?

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**Pierre-Jean Sivignon - Royal Philips Electronics - CFO**

Well as you know it's an industry which is difficult, but that being said for us it's a business model gain right? You start the sentence with very strong growth, but I will answer you with business model. I think all business model is 4 to 4.5% basically almost regardless of the strong growth. And if you look at our first quarter it's a quarter which is in line with that guidance and which gives us comfort on us meeting that particular target. So I prefer to basically put the emphasis on the business model and on the guidance of EBIT margin rather than on the growth because in that industry as you know sometimes growth can be your enemy.

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**Janardan Menon - Dresdner Kleinwort Wasserstein - Analyst**

Sure, but can I assume that you had about EUR50 million from you licensing in the quarter in earnings?

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**Pierre-Jean Sivignon - Royal Philips Electronics - CFO**

Well the guidance we've given to you is 1.5 to 2%, it's not 50 million it's more like 40 million -- around 40 million, that's I think the guidance we've given to you. And 1.5 to 2% on the year as a percentage of the total revenue, that guidance still holds.

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**Janardan Menon - Dresdner Kleinwort Wasserstein - Analyst**

Thank you very much.

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**Operator**

Thank you. The next question comes from Mr. Didier Scemama. Please state your company name followed by your question.

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**Didier Scemama - ABN AMRO - Analyst**

Yes good morning, it's Didier Scemama from ABN AMRO. Just a couple of questions, a few one-off actually, that's what I'm looking for. In terms of UK pension fund contribution of just short of 600 million, is that something that can continue in the next few quarters? Do you expect to have additional contribution or is it just a one-off and that won't happen again?

And my second question is regarding the other activities where you guide for an average quarterly loss similar to that of the first quarter. Can you maybe explain why that would not improve given the divestments that you've made?

And to finish off on the optical storage business, I'm not completely sure, have you totally got rid of the optical storage business or have you done additional divestments today compared to the press release that you had a few weeks ago?

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**Pierre-Jean Sivignon - Royal Philips Electronics - CFO**

Okay, I'll take them in sequence. The first one, on the UK it's definitely a one-off, we were underfunded. The reason why we decided to fund the UK is because the regulators there are taking a vested interest into this and there are possibilities that if you are not fully funded in that part of the world, regulator could be in the way of potentially for instance reorganization of a portfolio. So we had a -- I think we had lots of reasons to fully fund given that basically the evolution of regulation in the UK. But it's clearly a one-off and the one thing I will add is there, we have negotiated in a way where if the fund will be overfunded we would have the flexibility there in that particular country, so that's definitely a one-off.

On your second question of other, yes we've guided you on a year which should be algebraically four times what the first quarter is, and you're asking me, why isn't it better? Well as you know in that line it's a bit of a mixed bag which is precisely why we want to reduce it as quickly as we can. But in that mixed bag don't forget that we have real estate. And, now, last year because you know comparing year on year, I think when you say improvement I'm assuming you are referring to a potential improvement versus last year. And last year we had some gains, some extraordinary gains on the real estate and those things are not planned, they are not budgeted, I cannot count on them, I cannot exclude them for this year. But at this particular point we are guiding you on the four times what we had for the first quarter. That's the best I can give you at this particular point. Again difficult line to predict as you will agree with me.

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**Didier Scemama - ABN AMRO - Analyst**

Yes, no, definitely. But actually if I clean out, maybe I've not done the calculation right, but if I clean out for the exceptional gains and some special also one-offs in 2005 in miscellaneous order activities I get 271 loss so that would be roughly speaking flat in '06.

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**Pierre-Jean Sivignon - Royal Philips Electronics - CFO**

Well we've had -- I would have to come back maybe offline if you want more details on that particular line. I think we gave you -- I think [Gerhard Rosenthal] made a quick presentation back in -- I think in December or November where we gave you I think quite a bit of detail on that particular line so I'll send you back to the details. If you want more detail I think we can discuss offline. But I think the core of your questions would -- because we have a lot of exceptionals both ways between the two years, but probably what makes a difference between what you are expecting and what we are guiding you on is probably the real estate gain of last year. I think that would be my assumption, but we can discuss that one offline if you need more on that one.

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**Didier Scemama - ABN AMRO - Analyst**

Yes, no problem. Just to come back on my first question on the optical storage side. Are you completely out of optical storage now?

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**Pierre-Jean Sivignon - Royal Philips Electronics - CFO**

I think that once we've done -- once we've completed the BenQ operation on -- which will have that significant impact on the revenue with no impact on the margin as mentioned in a previous question, yes I think we will be almost completely out of optical storage.

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**Didier Scemama - ABN AMRO - Analyst**

And sorry to dwell on that again, but on the 67 million, once you're out of optical storage which is anywhere breakeven, what is the big delta then that we should be looking for because you also indicated that we should look for further divestments in the short term?

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**Pierre-Jean Sivignon - Royal Philips Electronics - CFO**

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Yes, just a correction because I think I am told by the real specialist of POS around me that we might -- we will still have, because it is classified as part of that automotive playback. So we will have still technically to be able to [thorough] we will still have one small portion which we are currently working on and hope to announce later this year. But let me say by the end of this year we should be done, but automotive playback post BenQ announcement should still be in our perimeter.

Now the two -- we will still be left with a portfolio between five and ten activities in what we call corporate businesses. And in this there are two, and in particular one which is still a bit of a headache for us. So I can't be much more specific, but we will do our very best this year to fix that problem, I can't be too much more specific, but we still have in there one headache.

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**Didier Scemama - ABN AMRO - Analyst**

Okay and just a final question just on a big picture. I think for the last six or seven years covering Philips I've never seen year-over-year growth rate of that strength across the business. Even if I take into account other activities it's still a very strong double digit. What's your feeling in terms of demand, and clearly it seems very strong, but what's your feeling there over the next nine months or so?

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**Pierre-Jean Sivignon - Royal Philips Electronics - CFO**

Well it's hard to be smarter than you guys are on that particular subject because you have more information. Everybody was scared about a weaker US in the first quarter; that hasn't really happened. So the good thing is if you look at the geographic split that we give you as part of the press release I think the good news is that our growth is actually evenly spread. As you could see pretty strong growth in Latin America, actually solid growth in Europe, on the back of Europe, which is doing if anything maybe a little bit better than planned if I listen to economic forecasts.

Asia is doing well, but really for us innovation; I think if I want to take some comfort, when I really drill down to that growth, when I look at Lighting, when I look at DAB, when I look at Consumer Electronics, when I look at Medical actually, all of them, and even when I look at Semi, all that growth really can find an explanation through or from innovation. If you look at Lighting, new products which we've introduced last year, if you look at Medical, look at our incoming orders, extremely strong, north of 15%, and there again on the back of a new product introduction.

If I look at Consumer Electronics we will have a brand range of LCD products introduced in the course of the second quarter, so this is still to come. If I look at DAP, we are still surfing on the new range of shavers which was completely renewed in the second half of last year. And for this particular year we are introducing a brand new range of epilators as part of DAP. So I can't really guide you more than we've guided you. What I can tell you is that we will definitely continue to innovate.

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**Didier Scemama - ABN AMRO - Analyst**

Thank you.

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**Operator**

Thank you. The next question comes from Mr. Thomas Brenier. Please state your company name followed by your question.

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**Thomas Brenier - Societe Generale - Analyst**

Good morning. Thomas Brenier from Société Générale. I have a general question on the restructuring in the acquisition related costs. If I calculate correctly for the Q1, these costs represent about 0.7% of sales. If I take the guidance for Q2 we would probably be in the region of 0.4%. Should we look at a recurring level around 0.5% for the whole Group going forward is there a time down the road, maybe in two, three years, where we could have a really lower impact from these kind of costs? Or should we really see them as recurring? Thanks.

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**Pierre-Jean Sivignon - Royal Philips Electronics - CFO**

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It's hard to guide you on this because it really depends on acquisition. I think we are totally transparent vis-à-vis you, and as you've seen we have introduced the concept of EBITA in our comments, and we've used the word EBITA in particular for Lumileds, so that you guys can actually run your math, and you can actually make the clear distinction between ongoing results and purchase accounting results which you know vocabulary includes not only the one-off acquisition cost, but as well the amortization of the intangibles. So now to guide you on what is going to be going forward, it's really hard, because it's totally depending on acquisition. I think what I can tell you is every time we acquire, we will give you very precisely what comes with the acquisition as soon as with our auditors we have discussed the split of purchase accounting and the goodwill and the impact of the amortization of intangibles, and we'll have to take it from there.

I think the numbers you have so far are being disclosed and are correct. Moving forward I think that's a tough one, but we will disclose to you, and keep in mind as well that we'll try to come up with acquisitions which are earnings per share accretive as quickly as possible.

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**Thomas Brenier - Societe Generale - Analyst**

Maybe I can be a bit more specific. I understand for acquisition related costs it's a bit difficult to forecast, but on the restructuring part of these costs, especially for divisions like Lighting, I have the feeling that these costs are becoming a bit more recurring than what I would have thought at the beginning. Can you comment on that?

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**Pierre-Jean Sivignon - Royal Philips Electronics - CFO**

No, actually no. Sorry, yes I can comment, but no they are not higher. The rules we have is that we normally disclose to you on a particular quarter for a particular product division when the cost is north of 10 million. I think that's the rule we followed. So for this particular quarter we ended up disclosing a couple of those, but in our forecast right now for restructuring, and I'm talking about restructuring, not purchase accounting, let's make the distinction there, our forecast for restructuring this year is in line, if not maybe a little bit lower than it was in '05. So no, nothing special there for this year.

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**Thomas Brenier - Societe Generale - Analyst**

Okay, thank you. Can I have another very short question, and I'm sorry if you already a bit answered a part of it. Q1 Group sales growth was in the region of 10% if we take comparable growth, and you still have guidance for the whole Group around 5, 6% annual growth. I understand maybe the comparison basis is tougher for the second half, but do you expect a kind of slowdown, or is it more that you want to be on the safe side?

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**Pierre-Jean Sivignon - Royal Philips Electronics - CFO**

No, I think we don't want to play games with you. We believe in the 5 to 6; we don't want to change anything there. As you know the Group has got a very strong seasonality. This quarter was stronger than you guys thought, probably a bit stronger than we thought, but 5 to 6%, in relative terms a strong fourth quarter is very much still what we want to stick to in terms of guidance. So that means that upcoming quarters obviously in order to be 5 to 6 with a 14% on the first one, clearly there will be an adjustment to meet the 5 to 6. So at this point of time we don't want to change the guidance.

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**Thomas Brenier - Societe Generale - Analyst**

Thank you very much.

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**Operator**

Thank you. The next question comes from Mr. Jonathan Crossfield. Please state your company name followed by your question.

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**Jonathan Crossfield - Merrill Lynch - Analyst**

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Yes, good morning. It's Merrill Lynch. My first question was on the LG Philips displays charge which you took voluntarily of EUR45 million. I appreciate this is only part of the capacity that's being closed down. Is there any chance that we'll see further charges like this coming through?

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**Pierre-Jean Sivignon - Royal Philips Electronics - CFO**

Okay, I think the story there is that you've used the word voluntary. I think it's exactly the way to describe it. We have -- the company doesn't belong partly any more to Philips at all. We have actually no obligation whatsoever. The equity, as you know, was written off in our books at the end of Q4, and the voluntary contribution was part of the elements that we had made available to the management in those particular countries; we had made a certain number of things at their disposal to accommodate the difficulty of the workers there. So that's the rationale behind that voluntary 45 million. Should there be more? I can't comment on that, but certainly not of a material nature for Philips, and today we very much stand by what we've told you at the end of Q4, which is that Philips is not exposed any more to this business.

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**Jonathan Crossfield - Merrill Lynch - Analyst**

Okay. And then just as a follow-up on Semiconductors. Your commentary on the orders and the backlog was that you're receiving orders for beyond the second quarter. Is that in any specific end markets, or what do you think's driving the lengthening of the order book?

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**Pierre-Jean Sivignon - Royal Philips Electronics - CFO**

Well, I think it was across the -- well let me say first, the rule of the game that we disclosed -- well we didn't disclose, we reiterated to you at the end of Q4, meaning no visibility, are very much in play today. We are today, mid-April, the visibility we have on our revenue of the second quarter of 2006 is probably at best today 50%. So this is to tell you that the visibility we have in that industry continues to be extremely short-term.

Now, to your question, what are the particular verticals which have if anything helped our first quarter to be better? As I have said, it's definitely a multi-market, and automotive and identification with a particular note on identification.

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**Jonathan Crossfield - Merrill Lynch - Analyst**

Okay. Thank you very much.

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**Operator**

Thank you. The next question comes from Mr. François Meunier. Please state your company name followed by your question.

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**Francois Meunier - Cazenove - Analyst**

Good morning, it's François from Caze. Just a question on the licensing income in Consumer Electronics. Could you give us a precise number, because it says it's more than last year, so I guess it's more than EUR32 million, but can you give a more precise number?

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**Pierre-Jean Sivignon - Royal Philips Electronics - CFO**

Okay, yes, I will give -- the precise number is 45.

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**Francois Meunier - Cazenove - Analyst**

Okay, thanks. And now for the target you have for the company as a whole of 5 to 6% top line growth and 7 to 10% EBIT margin. Now given the growth that you have at the moment, and I would say the lack of leverage on margins maybe in Consumer Electronics, would you think that it's more likely to be at the top end of the forecast for top line growth than at the low end of the EBIT margin forecast?

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**Pierre-Jean Sivignon - Royal Philips Electronics - CFO**

Well, I think -- let's talk about two things. First on the leverage of growth, I think we've added -- Philips has added about EUR1 billion of revenue year-on-year, and about -- if you count, about 120 million of EBIT margin. So it's north of 12% contribution, so is that good, is that bad? I think it could always be better, but I would say that this particular quarter in terms of margin is definitely a better quarter than last year, the same period of time.

Now to your question, which is really a question related to the mix. Could we see a situation where the vast majority of the growth comes from Consumer Electronics and then adding potentially an impact on or guidance on EBIT margin which I think is what really you are asking me. No, I think we stand by what we've told you. We've guided you almost for every product division on the growth of revenue we saw. The one product division for which we have not guided you in terms of revenue growth is precisely Consumer Electronics, because there the name of the game is to deliver the 4 to 4.5%, because that is definitely the target and that is definitely the challenge to stay there year-on-year, thanks to the business model that we have deployed there. So basically, no change to the 5 to 6 in terms of comparable growth.

In terms of EBIT margin, we want to go from the 5.9 of '05 to something between 7 and 10 in '07, so definitely the year '06 will have to be in the middle, and regardless of the respective weight of Consumer Electronics. So none of that is changing.

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**Francois Meunier - Cazenove - Analyst**

Okay. Thank you very much, Pierre-Jean.

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**Operator**

Thank you. The next question comes from Mr. Jan-Willem Berghuis. Please state your company name followed by your question.

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**Jan-Willem Berghuis - Kempen - Analyst**

Yes, hello, good morning. It's Jan-Willem from Kempen. My question is, you mentioned in the next two months the share buyback program will be formally finalized and that you also were reviewing the acquisition targets in Medical. Can you say what is your targeted balance sheet structure by the end of the year, in other words, how much room do you have to leverage up the balance sheet, in your opinion?

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**Pierre-Jean Sivignon - Royal Philips Electronics - CFO**

Okay. I think, just to say one word on the share buyback, technically we've acquired all the shares up to the 1.5 billion that was disclosed mid-August. And when we say it will be completed in the next two months we refer very specifically to something which is quite important for you analysts, which is the cancellation of the shares, because we are one of those companies which will ultimately cancel almost all the shares that we have bought back as part of that 1.5 billion. So this will be done for legal reasons over the next two months, and I think this will lead to a reduction of quantities of shares by up to almost 6% I think, which is obviously quite significant. So that's the first part of your question.

Second part of your question. Yes, we've mentioned in the press release that we will continue to look at our portfolio of acquisitions, and I don't think we mentioned Medical; I think we said portfolio of acquisitions, nothing new there. The domains we are looking at are the ones we've disclosed in the past so they are there, I won't repeat them, there's nothing changed. And at the time we use our cash in the coming quarters, we will look at those same three territories which is share buyback, dividends and acquisitions. I think on the back of Q1, as you've seen, we used quite a bit of money on pension, buyback and acquisition, actually if anything we've done exactly in Q1 what we said we would do as a rule.

Now, to the last part of your question. What is a good or optimized balance sheet structure for Philips. There again, no change. Our game is still to adhere to the guidelines of an A rating. We are as you know there for one agency, not quite there for the other one, still very much working on getting there for the second one, indeed, which is Moody's. And if you look at their game, even though that's not the only criteria, because there is one related to cash flow, but the one related to leverage is something which is about 20, 25% of your equity as a maximum amount of debt. Once -- and then you have to deduct obviously the underfunding of pensions and leasing. So I'll let you run the math and you can then calculate the outcome [it's going to be].

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**Jan-Willem Berghuis - Kempen - Analyst**

Okay. Thanks very much.

**Operator**

Thank you. The next question comes from Mr. Luc Mouzon. Please state your company name followed by your question.

**Luc Mouzon - Exane BNP Paribas - Analyst**

Hi, good morning. Just a couple of precise questions regarding the CapEx trend firstly. I know you integrate Lumileds you had an increase on the CapEx side. Could you give us maybe an update on the guidance for the full year, what you could expect for the whole envelope for the full year?

And a second question is coming after your answer on the previous question on the LPD. Should we understand that LPD is not considered as a financial investment as of the second quarter 2006, and will not be any more consolidated within the results from unconsolidated companies?

**Pierre-Jean Sivignon - Royal Philips Electronics - CFO**

Okay. I think as far as CapEx is concerned, we basically guided you at 1 billion. That was indeed before we integrated Lumileds. I think the new guidance on CapEx probably going to be closer to 1.1 billion; I think if you have to have a number, it's probably going to be 1 and 1.1, and as we see it today, probably around 1.1. You know, we usually are underspending on CapEx, as you know historically, but that's today probably the best guidance I can give to you.

Sorry, on LPD, can you -- ?

**Luc Mouzon - Exane BNP Paribas - Analyst**

Yes, LPD, as far as I understand, and from the way you present the results from unconsolidated companies within the Group, you consider [now] LPD as a financial investment, a bit like TSMC, you're not considering it as an associate any more. Is that correct or not?

**Pierre-Jean Sivignon - Royal Philips Electronics - CFO**

No, no actually LPD is completely out of our books. I think it's not considered as anything any more. It's actually not in our books any more.

**Luc Mouzon - Exane BNP Paribas - Analyst**

Not at all?

**Pierre-Jean Sivignon - Royal Philips Electronics - CFO**

No, not at all. Actually LPD for us is now absolutely deconsolidated and as I mentioned on a previous question, our legal exposure and financial exposure is zero, and what has taken place in Q1 was a voluntary move for the reasons which I just mentioned. But it's totally out of our books.

**Luc Mouzon - Exane BNP Paribas - Analyst**

So it means that there will be no other contribution whatever from a voluntary or from a legal point of view over the next quarter?

**Pierre-Jean Sivignon - Royal Philips Electronics - CFO**

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No, of course I cannot say that, because there might be, but they would not be material. I think we will leave to our managers in certain circumstances obviously some latitude and not necessarily by the way via cash. There are other ways to help the people, but we will only do it at our discretion on an exceptional basis, and certainly with no material impact on Philips.

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**Luc Mouzon - Exane BNP Paribas - Analyst**

Which means that you're planning to give the 15% you still own in the company to the managers, basically?

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**Pierre-Jean Sivignon - Royal Philips Electronics - CFO**

No, we don't own any more 15%. That 15% doesn't --legally and practically, that 15% doesn't belong to us any more. We don't own any more of LPD today.

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**Luc Mouzon - Exane BNP Paribas - Analyst**

Okay. Thank you.

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**Operator**

Thank you. The last question comes from Mr. Hermann Betten. Please state your company name followed by your question.

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**Herman Betten - Betten Beursmedia - Media**

Yes, good morning. Hermann Betten from Betten Beursmedia. Most of my questions have already been asked, but I would like to still ask you what the guidance is on the utilization rate in Q2, and as a follow-up on that if you would be able to give me the breakdown of the Semiconductor division as far as product lines are concerned? For instance, what's the part of communication as part of the revenue?

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**Pierre-Jean Sivignon - Royal Philips Electronics - CFO**

Well actually, in terms of guidance we normally I think do not guide you there; I think the actual utilization was 82%. I think the guidance we normally give to you on Semiconductors is beside the guidance on the margin, on the [better risk] for the margin, is the guidance on the revenue and I think that particular guidance is in the press release.

On utilization I think historically we've not guided you.

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**Herman Betten - Betten Beursmedia - Media**

And as far as the breakdown is concerned?

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**Pierre-Jean Sivignon - Royal Philips Electronics - CFO**

Well, I think in terms of giving breakdown for the second quarter?

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**Herman Betten - Betten Beursmedia - Media**

No, no, for the first quarter. What percentage of revenue was automotive and identification, for instance?

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**Pierre-Jean Sivignon - Royal Philips Electronics - CFO**

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Well, we normally -- let me give you maybe a little bit of light, but there either we normally -- let me go to the next one and I'll come back to that. If you have one more question, let me see what we can give to you in terms of macro trends on the Semiconductors.

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**Herman Betten - *Betten Beursmedia - Media***

Yes, thank you.

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**Operator**

Thank you Mr. Sivignon, there are no further questions.

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**Pierre-Jean Sivignon - *Royal Philips Electronics - CFO***

Okay, so then I will -- basically the two drivers would be -- let me try to put this right for you. If I combine -- I mean the largest would be mobile and personal, I think that's north of 30%. And the second largest would be multi-market north of 25%. The other two being I would say more or less comparable. That would be the split on the revenue of the first quarter. Okay?

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**Operator**

This concludes the Royal Philips Electronics First Quarter Results call on Tuesday April 18, 2006. Thank you for participating. You may now disconnect.

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