

FINAL TRANSCRIPT

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PHG - Q2 2007 Royal Philips Electronics Earnings Conference Call

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PRESENTATION

Operator

Ladies and gentlemen thank you for holding. Welcome to the Royal Philips Electronics' second quarter results 2007 conference call on Monday July 16, 2007. For the introduction by Mr. Pierre-Jean Sivignon, Chief Financial Officer, all participants will be in a listen-only mode. After the presentation there will be an opportunity to ask questions. (OPERATOR INSTRUCTIONS). Please note that this call will be recorded and is available by webcast on the website of Royal Philips Electronics.

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

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

Thank you. Ladies and gentlemen let me first welcome you to this conference call for the second quarter results of 2007 for Royal Philips Electronics. I will make a few introductory remarks and then open up the call to your questions.

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The second quarter was another successful step towards achieving many objectives which were designed to raise our profitability. Let me be more specific; EBITA in the quarter was EUR389 million or 6.4% of sales and this compares to 4.5% one year ago. This increase is another good step to achieving our target of above 7.5% for this year 2007.

Comparable sales growth for the company was flat for the quarter however our three high margin divisions to which we will be allocating more capital showed combined comparable growth of 7% with DAP once again at a very high level, 14%. These growth levels together with the expected improvements of Consumer Electronics in the second half of the year, support our annual average growth target.

In Medical Systems the comparable growth was 4% with strong performances in the majority of the businesses. Equipment order intake showed a 12% increase compared to one year ago and this improvement is in line with our projections three months ago. The EBITA percentage increased in the quarter in line with our expectations. As we mentioned a short while ago, we are currently reviewing our options for our shareholding in MedQuist and will inform you about this as soon as possible.

In DAP the excellent quarter has given us a 14% comparable growth following 17% in the first quarter which again more than supports our target of 7% which we expect to exceed this year. This very strong growth came in virtually all the product groups and geographical regions.

Looking at it another way, we can see three main drivers this quarter. Firstly the healthy living theme, secondly, product innovation and thirdly, emerging markets. EBITA of 13.2% in the quarter was strong and again shows that we are on track to achieve our target of 15% for the year.

Sales in Consumer Electronics on a comparable basis declined by 11%. The main reasons for this are first of all the expected change of seasonality due to the World Cup last year and second, the introduction of the new range of products late in the quarter. This is actually supported by the improved comparable growth experienced in the latter part of the second quarter. The decline came in Connected Displays.

It's important to note that the European sales in CE of flat television are driven by US dollar denominated supply. The downward impact on this is not reflected in the Q2 comparable sales of CE; taking this into account would bring the true comparable sales into a better light. We expect an improvement in the second half of the year as we get the benefit of what was working against us in the first half of the year. The EBITA margin at 1% was a little higher than one year ago and we remain on track for the 3% EBITA guidance for the year.

The Lighting sales growth was 6% and one of the main drivers that we are seeing emerging is a switch to energy saving products. We expect this trend to continue. The published lighting EBITA percentage was slightly lower than the second quarter of '06 due to acquisition related cost and restructuring so that the underlying performance of Lighting is progressing well.

The results for Innovation & Emerging Businesses was in line with our expectations, although slightly lower than in the first quarter.

In Group Management & Services we see the impact of our cost reduction plan as well as lower SOX cost. Pension and other costs were lower than we expected and the brand expenditures at EUR29 million was a little lower than we originally planned. We will complete our EUR75 million cost reduction program this year which will require a one-off cost of approximately EUR15 million to be incurred in the second half of this year.

The net cash in the quarter was EUR2.5 billion compared to EUR2.2 billion at the end of the first quarter. This change was mainly due to the proceeds from the sale of TSMC shares offset by the dividend payment and the share buyback. We are very pleased that the second trading line has been operational during the second quarter allowing us to buy back shares in a tax-free way. We are continuing our efforts to allow this to continue.

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The inventory percentage of 12.7% is 0.8 percentage points higher than one year ago. This is due to items of a temporary nature. There continue to be one or two areas where the inventory to sales ratio can be improved and we are working on them.

The results from non-consolidated companies have swung to profitability based on the improved performance of LG Philips LCD. We continue to look for acquisitions in the area that we have designated that will add value in line with our guiding principles.

I reiterate our intention to have leverage on our balance sheet within two to three years consistent with our rating objectives. We once again confirm our sales growth target of an annual average comparable growth of 5% to 6% and an EBITA of above 7.5% for 2007.

Let me now open the call for your questions.

QUESTIONS AND ANSWERS

Operator

Thank you sir. (OPERATOR INSTRUCTIONS). The first question comes from Mr. Niels de Zwart from Rabo Securities. Please go ahead with your question.

Niels de Zwart - Rabo Securities - Analyst

Good morning. Niels de Zwart, Rabo Securities. My first question would be on your capital reallocation. I saw some headlines on the wires that you're planning to reduce your stake in LPL to below 20% for this year and you're willing to sell NXP [down]. Could you comment a bit on that?

Pierre-Jean Sivignon - Royal Philips Electronics - CFO

Yes, I think on LPL there is nothing new. I think we said that we would want to go below 20% at LPL as the first step, post the lapse of the lockup period which as you know will actually be mid-July, so it's almost now. So there indeed we would like to go below 20% and we will focus on that. Nothing new, that's in line with what we had announced in the previous quarters.

On NXP, no I think there is nothing new on NXP, I think NXP is not one of our priorities. There as you know we're not in the driving seat, we have no lockup on NXP. We're not particularly anxious to sell that particular one. As I mentioned this morning we will be opportunistic but that's not one of our priorities right now, definitely not.

Niels de Zwart - Rabo Securities - Analyst

And a follow-up on Consumer Electronics. Could you maybe tell us something which you see going on in the market in return -- in relation to inventory positions within the channels? Would you see that developing at the moment?

Pierre-Jean Sivignon - Royal Philips Electronics - CFO

Yes I think it's hard for me to comment on the sector because as you know we normally don't do it. Our model is a model which tries precisely to put us in a situation where we don't have to comment on the sector in general. What I can say on Philips is that our inventory basically is down. I think Consumer Electronics is one product division which saw its inventory expressed as a percentage of revenue come down in Q2 '07 versus Q2 '06. So I would say that we are ready to attack the second half of the

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year. And the other thing which I think is important is that we started introducing innovation late in the second quarter and we will be basically capitalizing on this innovation for growth in the second half of the year and that was indeed disclosed in the press release.

Niels de Zwart - Rabo Securities - Analyst

Okay, maybe one quick question. During your analyst meeting you mentioned the impact you expected from the Deficit Reduction Act in the US on your revenues in Medical Systems. When we saw GE last week they mentioned a stronger than expected impact. Are you seeing the same or are you still seeing the impact you had foreseen a couple of months ago?

Pierre-Jean Sivignon - Royal Philips Electronics - CFO

No I think we are very consistent. We gave you a number -- a ballpark figure number last quarter which was saying that it could have up to 1% potential impact, maybe slightly more maybe, but around 1%. Nothing has changed. The US is a difficult market right now for the particular modalities which are exposed to this budget reduction Act and there we really had no surprise. I think what we said at the end of Q1 was that the second quarter should show an increase of our incoming orders rebounding which is evidenced now with that 12% increase. And the one thing I want to say is that in the United States, as part of that 12%, in the modalities not impacted by the budget reduction Act we did well. So I think in Q2, in the non-impacted modalities in the US, we had a good performance in incoming orders and we had a good performance as well out of the US given that now that business is a truly global business at Philips.

Niels de Zwart - Rabo Securities - Analyst

Okay, thank you very much.

Operator

Thank you. The next question is from Mr. Janardan Menon from Dresdner. Please state your question.

Janardan Menon - Dresdner - Analyst

Yes, hi. Just to follow up on the Medical question. When you say that you're not doing well in the larger modalities, presumably CT and MRI is what is being affected in the US. So if your second half continues to see that trend and your upturn is mainly driven by patient monitoring and ultrasound and things like that, would that lead you to a slightly lower margin trajectory into the second half given that you do make higher margins on areas like CT?

Pierre-Jean Sivignon - Royal Philips Electronics - CFO

No, I think CT was mentioned, yes, essentially in the US, so that's -- by the way that was something which was there as well if you remember in the first quarter. But the modalities -- the emerging modalities in the rest of the world actually offset the US. So, basically as far as imaging is concerned, the situation in the US which is known, which was indeed commented by GE is there. There is a -- I think you know just about our exposures there, we've described it in Q1 and we maintain it in Q2. But the rest of the world is indeed helping; Europe is helping certainly in imaging in the second quarter. But I think the important thing is that, in the US, the other modalities, did well. So all-in-all our situation in the US combining all the portfolio actually was probably better than what was described by some of our competitors.

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Janardan Menon - *Dresdner - Analyst*

Okay. And just --

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

So I'm not -- and to your conclusion, no we're not changing. I think to the question at the end of Q1, should we change guidance on EBITA and the answer was no. And today at the end of the second quarter the answer is still very much as we mentioned at the analyst's conference; we stick to our guidance for Medical. And on the back of that 12% incoming orders, if anything we take additional comfort from that.

Janardan Menon - *Dresdner - Analyst*

And just a question on your top line growth. You've said that it's 5% to 6% average annual sales growth. How does that reconcile with the ongoing weakness in Consumer Electronics? Is it that at some point do you expect Consumer Electronics to stabilize and start growing to help you achieve that? Or how do we sort of reconcile those two trends?

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

Well I think the answer is yes. Well actually the answer is yes plus a few other things. We expect CE to rebound in the second half of the year, I think that's your point. The other product divisions are doing well, I think all the other product divisions are growing nicely. The guidance there has been confirmed so we expect to have a stronger part of the year in terms of growth in order indeed to be able to deliver on the average annual guidance that we've given to you for the revenue, indeed.

Janardan Menon - *Dresdner - Analyst*

So you think you're going to achieve that for this year as well?

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

It's an average, so as every average it can be a little bit up, a little bit down. It's an average over a couple of years so I think we stick to that guidance which has been there for quite some time and there is nothing new there. So we will need some growth in the second half to stick to that guidance and that's what we expect.

Janardan Menon - *Dresdner - Analyst*

Okay, thank you very much.

Operator

Thank you. The next question comes from Mr. Simon Schafer from Goldman Sachs. Please state your question sir.

Simon Schafer - *Goldman Sachs - Analyst*

Thank you very much. I wanted to ask a follow up question on the LG stake. Obviously in the past there have been some differing opinions or comments as to whether this would be a corporate buyer or the public. I was wondering whether you could remind us what your preferred exit route would be between the public and a corporate buyer? Thank you.

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

Well the aggregate is value. I think it's very hard to comment on I would say selling strategies and target prices because as you know, this is begging for trouble. I think what we've said is that the avenues -- the traditional avenues which is a placement, which is a strategic buyer or even private equity, those are solutions that are open. And to tell you where our preference would go is something I don't want to do because I think I want to keep for ourselves the maximum latitude vis-a-vis the particular objective that we have given to ourselves. The driver is value.

Simon Schafer - *Goldman Sachs - Analyst*

Understood, okay. And a question on the Lighting business. You've made I guess three recent acquisitions in solid state lighting now; PLI, TIR and Color Kinetics. So it seems like you've done a good amount of bolstering up. Is there anything else that you think you need to bolster up on in that specific area or is that what we need to do for now in solid state lighting?

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

I think in solid state lighting we've made some important strategic as well as tactical acquisitions. I think it's a sector we will continue to look at because I think having IP, having capabilities to grow in that sector is of paramount importance, in particular given the growing role of SSL; solid state lighting in green lighting. Could we do more? I can't guarantee it. Will we continue to look at SSL? Most definitely.

I think as far as lighting in general is concerned we'll continue to look at lighting and the lighting adjacencies because we believe that's it's an important part of Philips; we are clearly leaders. And with the trend currently influencing the world, whether it's cost of energy or the attention -- increased attention to green lighting, we all the more believe that it's a sector we need to spend increased attention on. So I think we'll continue to look at the complete sector in the quarters to come.

Simon Schafer - *Goldman Sachs - Analyst*

Understood. Thank you. And my last just brief question on the share buyback on the second line. Contrary I think to expectations perhaps, you've now done 45% of the amount that you'd like to complete, that was the EUR1.6 billion this year. So if you continue to execute at the current run rate there's probably room for upside in terms of adding to this program. I was just wondering as to how you feel about being able to do more in later stages of the year?

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

Yes I think to the first part of your question, we had a slow start for various reasons. I think we were confident we would move on and the good thing is that we have indeed experienced that acceleration and we are confident that we will be able to deploy that 1.6; slightly north of EUR1.6 billion this year.

As far as additional share buyback is concerned, I have no further declaration to make today. But keeping absolutely focused on the capital redeployment as you know has been one of our constant focus, but nothing else to add at this particular point of time today.

Simon Schafer - *Goldman Sachs - Analyst*

Okay, thank you very much.

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Operator

Thank you. The next question comes from Mr. Andreas Willi from JP Morgan. Please go ahead with your question.

Andreas Willi - *JP Morgan - Analyst*

Good morning. The first question I have is on the US Medical business. What do you see there in terms of pricing for products in the modalities that are affected by the Deficit Reduction Act?

GE talked on Friday about taking out costs in that business, assuming to improve competitiveness there maybe. Maybe reduce prices to stimulate growth again. What are you seeing in that business?

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

No I think - yes, just like you we read very carefully the announcement of GE on Friday. I think it's -- the explanation which we gave at the end of Q1 still stands. We are probably less exposed than some of our competitors to the non-hospital world in the particular domain of imaging. And I think that is probably something which is helping us in that domain.

As far as taking cost is concerned, we have no particular plan to do more than A, the regular plan which we had announced across the whole of Philips. And if you remember, at the end of last year and at the beginning of this year we announced that we were trimming off our costs in our selling organization in North America. That is something which dates back almost now to a quarter. That's done; that plan has now been totally executed. We are starting to get the impact of that reduction of our selling expenses in the US and at this particular of point in time we are comfortable with that action plan.

Andreas Willi - *JP Morgan - Analyst*

And my follow-up question just relates to the innovation in emerging businesses there. Maybe the guidance for the negative EBITA amount is maybe slightly higher than before, but you're saying the run rate of the first half should be expected for the second half. Could you just give a little bit more color what has changed there?

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

Yes I think two -- yes I think all what you're saying is absolutely correct; two things have changed. One is that we are spending in order to speed up actually what's happening in the incubators as well as in central research. We are spending more money than what we have planned in incubators and you will have the opportunity to talk more about that when we have our analyst conference in Eindhoven, I think on September 28. You'll have more color on what's happening in that particular territory.

And the other thing which has changed is that we have some IP income in that particular part of our income statement and that IP income has actually come down compared to what we're expecting. So that's why we are guiding you now on a line which will be still well lower than last year but a bit higher than the previous guidance that we had given to you so far.

Andreas Willi - *JP Morgan - Analyst*

Thank you.

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Operator

Thank you. The next question comes from Mr. Julian Mitchell from Credit Suisse. Please state your question sir.

Julian Mitchell - *Credit Suisse - Analyst*

Yes thanks. The first question is really regarding your selling costs for the company as a whole. You saw your revenues fall 4% in the second quarter but your selling costs are up about 7%. Could you explain a little bit where you're spending and how much you see selling costs increasing for the year as a whole and in the second half? Thanks.

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

Yes the selling expenses were up. A big reason for that is the change of the perimeter. We had a couple of acquisitions which came up with higher selling expenses and that's a big part of the explanation expressed in percentage. So I would say a lot of it has done -- has to do with the mix.

Julian Mitchell - *Credit Suisse - Analyst*

Okay, so that 7% increase probably won't be repeated in the second half because you'll be integrating the acquisition costs?

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

Yes but in the domain of Lighting, for instance PLI is coming up with a higher level. The structure of the PLI income statement is a bit different from what we know in the rest of Lighting and there we have, as you remember it's a business which addresses consumer markets and that is coming up with higher selling expenses than the average of Philips and certainly of the average of the Lighting product division. That's I would say the main reason.

Julian Mitchell - *Credit Suisse - Analyst*

Okay, thanks.

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

The other one probably would be DAP. That is one which will correct itself. I think we've told you in the release that DAP is coming up with a lot of innovation in the second half. We have a brand new line of shavers which is called Arcitec which will see -- which have actually started shipping as we speak. And we have some selling expenses on the back of that.

And the other thing as well is we are launching a brand new range of oral healthcare which I think will be there in August of 2007 so that probably is the other reason. But that one I would say is much more, I would say punctual and will disappear on the back of the introduction of those products.

Julian Mitchell - *Credit Suisse - Analyst*

Okay, thanks. And just a quick follow up in terms of your corporate costs. You saw a big reduction year-on-year in your core corporate cost line. Do you think you're now at a stable run rate for the second half versus what we saw in the second quarter? Or do you think we might see further increases still in terms of efficiencies there?

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

No, I think the reduction of corporate costs is for real. A lot of it has to do with last year we had IT costs as well as Sarbanes-Oxley costs. I think we had guided you on a reduction of that and we are benefiting from this reduction, particularly in that second quarter.

The other thing which helped us in the second quarter was the reduction of pension costs and there we guided you in the press release. Do we have now a stable amount? Yes, I think the guidance we gave you basically, which was if you remember, the 50 basis points on the Group management services, which is what we call the headquarter costs plus the amount we gave to you on pension and the ballpark figure of 110/115 on the brand, I think that is pretty much the guidance for the year and we stick to it.

So I would say a reduction of costs there, as indeed I would say it's for real, it has stabilized.

Julian Mitchell - *Credit Suisse - Analyst*

Okay, thanks.

Operator

Thank you. The next question comes from Mr. Jan-Willem Berghuis from Kempen. Please state your question sir.

Jan-Willem Berghuis - *Kempen & Co - Analyst*

Yes, hello, good morning. I just wanted clarification, you mentioned the 5% to 6% comparable growth for the overall Group for this year is an average number. The 6% Medical target, that is a target for 2007. Is that a hard target or is it also an average?

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

No, that's our target. I think if you -- the guidance of Philips if our target for three PDs out of four; that one PD being Consumer Electronics for which you have a hard target in EBITA percentage. And the target for the revenue is an average annual growth of 5 to 6. So the PDs are a hard target for the year -- sorry, the Philips altogether is an average 5% to 6% organic.

Jan-Willem Berghuis - *Kempen & Co - Analyst*

Okay, thank you.

Operator

Thank you. The next question comes from Mr. Sean Murphy from Nomura. Please state your question sir.

Sean Murphy - *Nomura Securities International Inc. - Analyst*

Good morning. I have some questions about MedQuist. It sounds like some of their accounting problems are getting fixed but I think you've also been quoted as being maybe aggressively looking to reduce your stake in the company, so could you comment please?

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

Yes, I think we -- if you remember we started getting current -- actually I should let me be very precise. We started publishing -- I should be even more precise. MedQuist started publishing results already some time ago, but as you remember, those numbers were not current vis-a-vis SEC. So this particular quarter show a major milestone having the accounts now being not only published but properly filed vis-a-vis SEC up to the year 2005. So we still have to work on '06 as well as the first quarter of '07 and that's obviously being very actively worked on. And this is indeed completing a couple of years of hard work to get these things back to where they should be.

Now to the second part of your question. Are we actively pursuing? I think we are, obviously, on the back of accounts which are now almost totally current getting some proposal at the Philips level, but we know as well that at the MedQuist level some proposals have been received and at both levels those proposals are being looked at yes.

Sean Murphy - *Nomura Securities International Inc. - Analyst*

Okay, thank you.

Operator

Thank you, the next question comes from Mr. Luc Mouzon from Exane BNP Paribas. Please state your question sir.

Luc Mouzon - *Exane BNP Paribas - Analyst*

Yes, hi, good morning. Just to come back on the Consumer Electronics situation. If you might comment a bit further into what you expect for the second half of this year because I understand there is an ongoing pricing issue when it comes to the TV market, especially coming from your Japanese competitors.

And you made some comment about the US currency driving further down this market. So I would expect the second half very much to depend on the new product pipeline but also on maybe some initiatives.

And to extend that question to the EBITA target that you got, 3%, what could be done on the top of your already asset light situation and the fact that you are very small with very limited number of plans. What could be done to very much boost that margin towards 5% to 6% in the second half, in order to reach that target?

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

I think you have asked three questions. Let me start with the number two which is the exchange rate. We always comment on an organic basis, which is clean of ForEx fluctuations. So when we comment on Consumer Electronics and it's always away from the impact of exchange rates. So let me, for the sake of the rest of the answers, let me go away from the ForEx element.

Now the first question is do we need to grow in CE in Q3 and Q4? The answer is yes and I think that's what we plan. We have a lot of new products coming up in the second half of the year and what I said earlier on today was that if you zoom on the profile of our revenue in the course of the second quarter, we saw a quarter where in the latter part of this quarter, the trend started reversing. And that has to be linked obviously to the fact that late in that quarter we did introduce some innovation. So that's for Consumer Electronics.

And basically as far as the profitability of Consumer Electronics is concerned, this business is extremely seasonal, as you know. A lot of the CE sales comes in the fourth quarter; Thanksgiving, Christmas are all driving sales in an extremely important manner.

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There is nothing new, it has been the story of that product division for quite some time. As well as for, obviously, consumer businesses in general and the fourth quarter will be, indeed, the one which will make it happen to the 3% combined on the back of the 1% we've had so far. Because obviously volume in that business has an impact even if, as you've mentioned, our asset base has been drastically reduced. Fixed costs still have to be absorbed and the volume does trigger a higher EBITA margin in the latter part of the year.

Luc Mouzon - *Exane BNP Paribas - Analyst*

So just to follow up, it doesn't mean that you need anything to be added in terms of whatever restructuring action or specific actions to reach that 3% EBITA target?

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

No, the answer is no. And moreover, as you know, we always comment on margin at constant perimeter, so if we were to do something, we would have almost to re-discuss with you guidance. The 3% guidance we give to you is with the existing perimeter.

Luc Mouzon - *Exane BNP Paribas - Analyst*

Okay, thank you.

Operator

Thank you, the next question is from Mr. Didier Scemama from ABN Amro. Please state your question sir.

Didier Scemama - *ABN Amro - Analyst*

Good morning gentlemen. I just have one question and a couple of follow-ups.

First of all, if I look at the margins in Lighting, we see a bit of a deterioration versus the first half of '06 and I was just wondering if you could comment on the underlying reasons for that?

And I have a couple of follow-ups. One regarding the share buyback. If you could maybe talk us through maybe the initiatives you're taking with the Dutch tax authorities to loosen up a bit the regulations regarding tax free buybacks, that would be very helpful.

And finally, on the reallocation of capital, are you still looking at a 60/40 split between acquisition and cash return to shareholders? That would be great.

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

Okay, alright. First question on Lighting, yes you are correct. We end up with an EBITA at 11% -- reported EBITA at 11% versus 11.5% last year but we had -- in the 11% we have a one-off of EUR11 million which relate to inventory -- one-off inventory charges in PLI and that charge is not canceled in EBITA. So this is having a direct impact on EBITA.

And the other element is that we had in that EBITA of 11% EUR7 million of restructuring charges which is actually ahead of the restructuring charges that we had last year. So if you combine those two elements, you will calculate backwards that the charge -- excuse me the EBITA percentage margin at Lighting is actually up like-for-like.

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On the second question, which is the initiative we have with the Dutch tax administration, I think on the second trading line we use, obviously, the law and certainly we are in total clarity with the Dutch tax authorities. And via a succession of specific rulings, we got that second trading line to start moving. And you could see that in the second quarter it did move and we did get traction; we are now, I think, 40% to 45% of the way. Are we doing more things? Of course, as any organization in this country, we are having negotiation to lower the tax burden in terms of capital reallocation. It's hard to comment much more obviously, but you can be confident that we were working and are continuing to work on this particular issue which we consider as essential for Philips and companies here in the Netherlands.

Your third question relates to the split. That split of 60/40 is i.e., 40%, actually a bit south of 40% for acquisition and 60% for the rest being dividends, buyback and pension plan refunding. That is the calculation which has been done on the last, almost two years. We've always resisted giving some guidance moving forward, not because we don't want to, but because if we do that we almost put ourselves in a situation where we give ourselves a budget to spend on acquisitions which is something we've always refused to do. And as you know on acquisition we've been always opportunistic; you saw this quarter us coming up with a list of small tactical as well as strategic acquisitions and we will continue to do so. So I think that split of 60/40 relates to the past but we haven't given guidance as far as the future is concerned.

Didier Scemama - ABN Amro - Analyst

Right. And just to come back to the discussion with the Dutch tax administration. I understand that it's sort of a touchy subject but is there any confidence on your side that a proper solution can be found in the next 18 months?

Pierre-Jean Sivignon - Royal Philips Electronics - CFO

I'm sure you will, I'm sure -- Didier you're asking me an impossible question. I think -- let me say that we are working very hard at obviously smoothing and easing the tax situation here. I think that's all what I can say at this particular point. It's not for me to comment in the name of the Dutch tax authorities, I'm sure you will appreciate that.

Didier Scemama - ABN Amro - Analyst

No I understand that. In any case, I guess we should assume that the capital return to shareholders will continue via the second trading line.

Pierre-Jean Sivignon - Royal Philips Electronics - CFO

Yes. I think you remember when we announced that line in Q4 there was a lot of doubt because it's a system which had been used in an unsuccessful manner. We said at the time that we would work extremely hard, which we did; we had a number of sessions to clarify and got -- and finally got actually two rulings; one of them being actually a public press release by the authority themselves. And we'll continue to do that, work hand-in-hand in total clarity, completely in the open in something which obviously makes sense for everybody. So I think that's what we've done and that's what we will be continuing to do. And obviously communicate to you on an appropriate basis.

As far as the second line is concerned we will continue and obviously continue to look at the proper capital reallocation to shareholders in the quarters to come.

Didier Scemama - ABN Amro - Analyst

Quickly last one. If you can just share with us new products you're looking at for the second half in CE that would be great?

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

No, no absolutely. I think in CE, I mentioned that we have an extension of -- you remember Ambilight which is a product which is certainly different in the domain of flat LCD and plasma television. We have a product which has a particular, I would say, characteristic in terms of viewing experience. And you will see an evolution of Ambilight in the course of Q3 which certainly will catch the interest and the attention of the market. So that's for CE. But the whole line of LCD television will be renewed and we have as well new products in the domain of entertainment solution.

So that's not only CE. And of course on the peripheral accessories as well, come up with the new territories. It's not only new products coming from the acquisition but the line of peripheral accessories will be largely renewed.

And finally as I just mentioned, DAP is going to come up with a significantly renewed portfolio as I just mentioned in an earlier question on the back of Q3 and Q4.

Didier Scemama - *ABN Amro - Analyst*

Okay thanks.

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

So a lot of -- I think we can add probably a higher content of innovation in that second half.

Didier Scemama - *ABN Amro - Analyst*

Brilliant, thanks very much.

Operator

Thank you. The next question comes from Mr. [Alex Thurler] from Merrill Lynch. Please state your question sir.

Alex Thurler - *Merrill Lynch - Analyst*

Hi it's Alex Thurler from Merrill Lynch. I have two questions, one on Medical. Could you just tell us if you've benefited either directly or indirectly from this -- from the FDA issues in GE's OEC business? If you perhaps can quantify that? And then I have a follow up question.

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

Yes, I think the answer is yes. In one of the modalities we benefited from the particular situation you described. Was it significant? No. I think did we benefit from it, both in terms of revenue and to some extent orders in the US? Yes. But I wouldn't call it a major event.

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Alex Thurler - Merrill Lynch - Analyst

And then, I guess, the follow-up is, if you talk about the 6% growth in Medical, I think most of that would come simply I think, you have lower comps coming in the second half of '06 versus second of '07. So could I understand that if you just keep today's trend growth you will be very close to reaching your 6% target for the year?

Pierre-Jean Sivignon - Royal Philips Electronics - CFO

No, I think the 6% growth comes from a couple of things. It comes from basically continuing to increase our service business, which as you know is important because it has an impact not only on the revenue growth but it has an impact on the mix of margin. But it's coming as well from obviously having made that 12% increase of the incoming orders in that second quarter, that's really the key. Because in order to make 6% what I normally use myself internally as a back of envelope checkpoint is to have equipment incoming orders as an average to grow across the year by 6%. If you do that, you have a pretty good chance at making 6% revenue increase for the year.

Alex Thurler - Merrill Lynch - Analyst

Okay.

Pierre-Jean Sivignon - Royal Philips Electronics - CFO

If you look at incoming orders combined for Q1 and Q2 on equipment, you combine the two, semester to date you will see that we are north of that 6%. So that's probably where you get some comfort on the 6% growth revenue for Medical this year. .

Alex Thurler - Merrill Lynch - Analyst

Okay. And then in DAP, could you perhaps clarify the launch pattern of the new shaving and oral healthcare products? I think you were going, in the United States, first at least with the shaving product. How long that will take? And then what are the -- what's -- if you can give us either the percentage terms of margin or absolute costs in regard to this kind of launch?

Pierre-Jean Sivignon - Royal Philips Electronics - CFO

Okay. Shavers was -- as we speak shavers has started; I think the very first shipments must have left. I don't know if they are in the shops already. We have started spending money on communication as was raised on previous questions. So we will have, I would say, higher selling expenses in Q2 that's done and probably in Q3 as well. But I don't want to blow it out of proportion because this is part of the model of 15% to 16% EBITA margin at DAP. For basically toothbrushes and oral healthcare I think there the new products will come in August, I think. I think it's later in the third quarter.

Alex Thurler - Merrill Lynch - Analyst

But the selling expenses you've mentioned, I would have thought that most of those would come in Q3 and Q4 rather than Q2. Would that be correct say for shavers in particular?

Pierre-Jean Sivignon - Royal Philips Electronics - CFO

No because when you do those launches you always have to communicate ahead of them and as you know a lot of our communication first of all tried to [differentiate] from the product itself and focus on the brand because that has been angled,

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that's why it's somewhat, I would say, disconnected from the actual product when the sale is really happening. And as far as the selling expenses which are directly related to the sale, we try to do that ahead of the -- or slightly ahead of the launch in order to basically -- when you are a leader to tell the market that the new product is coming in. And in the case of shaving where we are obviously a clear leader, it's important to let the market know a little bit ahead of time.

Alex Thurler - *Merrill Lynch - Analyst*

Okay thank you.

Operator

(OPERATOR INSTRUCTIONS). The next question comes from Mr. [Harm Lutterhead] from Bettern Financial News. Please go ahead sir.

Harm Lutterhead - *Bettern Financial News - Media*

Good morning again. Just one question on the impact of the Deficit Reduction Act on Medical Systems sales in the US. Could you tell me what the impact was in the last quarter and what -- how this Act will affect the sales in the next quarters?

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

Yes I think to be completely specific, in Q1 -- we're talking revenue, we're talking revenue compared to what we could have normally have expected. I would say that in the first quarter the impact was 1 percentage point of revenue and in the second quarter you could say probably a bit north of that, 2 percentage points of revenue -- between 1.5 and 2 percentage points of revenue to be absolutely specific.

Harm Lutterhead - *Bettern Financial News - Media*

Alright, so that's minor -- well. And for next quarters will it be in the same order?

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

Yes I think we've used over the full year, we used at the end of Q1, 1 or slightly north of 1 percentage point of the total. I think maybe today it's between 1 and 1.5 I think. We have to look at what GE is saying as well, I mean they obviously have a perspective on that as well. But in our particular case, as I mentioned, we haven't really changed our view on this particular point versus Q1, but maybe the impact on the revenue was a touch stronger as I just mentioned versus what it was in the first quarter.

Harm Lutterhead - *Bettern Financial News - Media*

And how much of your sales come from the US, of total sales?

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

Yes it's all in, including the Service business, including MedQuist, all in it's about 50%.

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Harm Lutterhead - *Bettern Financial News - Media*

50?

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

Yes.

Harm Lutterhead - *Bettern Financial News - Media*

So 5-0?

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

5-0.

Harm Lutterhead - *Bettern Financial News - Media*

Excellent, thank you.

Operator

Thank you. You have a follow-up question from Mr. Niels de Zwart from Rabo Securities. Please go ahead with your question sir.

Niels de Zwart - *Rabo Securities - Analyst*

My question is basically more of clarification. Your EBITA margins are at least 7.5% dead. The reel refers to the EBITA as you have been promising that in your quarterly results or including some of the restructuring charges on other items you have been including in that number?

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

No I think we -- the EBITA guidance is all in.

Niels de Zwart - *Rabo Securities - Analyst*

That's all in? Okay thank you very much.

Operator

Thank you. The last question comes from Mr. Didier Scemama from ABN Amro. Please state your question sir.

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Didier Scemama - *ABN Amro - Analyst*

Yes I have a follow-up on Lighting. In the last week I think you had a press release regarding Epistar and ITC decision to prevent importation of products infringing your patents. I was just wondering, I mean do you expect a settlement with Epistar and if so, can you maybe quantify that? And are you going to aggressively, basically go after the other Taiwanese companies infringing your patents?

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

Didier you catch me there. I have to say I don't know. I would have to check on that Didier, I don't know. You know you are asking for something quite specific, I could not answer you. Let me look at this particular point, see if we can quantify it because what you want is -- what we have to say is in the press release. You are asking for numbers. Let me see if I can come up with numbers and come back to you offline. At this particular point right now I would prefer not to give you something which I'm not sure of. I'll come back to you.

Didier Scemama - *ABN Amro - Analyst*

Okay thanks.

Operator

I apologize, we do have one further question from Mr. [Matthias Chivers] from Dow Jones. Please state your question sir.

Matthias Chivers - *Dow Jones - Media*

Hello it's Matthias Chivers from Dow Jones. I have a question regarding acquisitions that have been done in the last year; one is regarding Lifeline. I was wondering if you have -- can already say when you will roll out this product to Europe for example?

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

Okay. Well first of all let me say, and I think it's in the press release that Consumer healthcare solution which is essentially including Lifeline, was up 16% I think in the revenue -- 15% in revenue in the second quarter. First quarter last year -- first quarter this year was up 16% so Lifeline is actually growing very nicely where it is today which is North America, essentially Canada and United States. As far as bringing it to Europe we are looking at various options. It's hard to give a date right now because what we find in Europe is that the market is actually a sigma of markets, and we are looking at them one by one, deciding to focus on a couple of countries more than others. But it's a bit early to say something more right now, but we are indeed working on it.

Matthias Chivers - *Dow Jones - Media*

But apparently it's hard to just roll out the product as it is in the US at the moment?

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

No, but, well it depends what you call the product. The concept can be brought to Europe. I mean the concept of actually helping or monitoring elderly people via a phone line, that is absolutely rollable or duplicable in Europe. The thing which is, as well, obviously leverageable is the back office. One of the elements of the value of a company like Lifeline is back office which enables

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you to do a tracking of all the calls in an extremely specific manner, I would say almost legalistic manner. All those elements can be leveraged.

Now to do it in a broadband manner as it is done right now in North America is difficult in Europe because as I said, the way elderly people are being taken care of in Europe is almost a country-specific approach. There is a lot of control elements there.

Matthias Chivers - *Dow Jones - Media*

Okay was this anticipated when you did your acquisition or is this something you find out along the way?

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

No I think when we made the acquisition we knew that we would do two things. A, we would increase the portfolio of products and that is something that we are currently doing, and we will come up with announcement there. The second thing we knew is that we would do a follow-up acquisition in North America which in the meantime has been announced, it's a company called Health Watch, so that obviously just gives us even more scale in North America. And what we said as well is we would look at introducing the concept in Europe, and we basically are currently looking at that. But the success of Lifeline and Health Watch, and of the sector in general, I would say it doesn't need a roll up in Europe to be accretive to the capital actually invested in that particular acquisition.

Matthias Chivers - *Dow Jones - Media*

Okay. Then one final question about AVENT. Are you considering to re-brand that into a Philips or are you adding Philips to the products -- the Philips brand? And when is that scheduled?

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

It's actually done. If you -- I think if you go to all the countries in the world which are selling the AVENT products you should see the new packaging worldwide now where the product is called Philips AVENT. So Philips is there now everywhere and it will be kind of a core branding approach like we still do for instance in the US. If you look at the shavers of Philips, Norelco is still very much on the packaging; you have Philips and then Norelco. I think in the case of AVENT that's what we've done and as we speak it's I think deployed all across the various countries where we sell.

Matthias Chivers - *Dow Jones - Media*

Okay thank you.

Operator

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

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

Thank you very much. Goodbye.

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Operator

Thank you. Ladies and gentlemen this concludes the Royal Philips Electronics second quarter results 2007 conference all on Monday July 16, 2007. Thank you for participating, you may now disconnect.

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