

Focus on Growth

Arthur van der Poel
CEO

June 21st, 2000

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Contents

- **Introduction to Philips Semiconductors:**
 - Who we are
 - The semiconductors market and key trends
 - Positioned for growth
- **Recovery in 1999**
- **Current status**
- **Vision and ambition**
- **Building on earlier strategy**
- **Focus on growth**
- **The four cornerstones**
- **Market outlook**
- **Industry consolidation**

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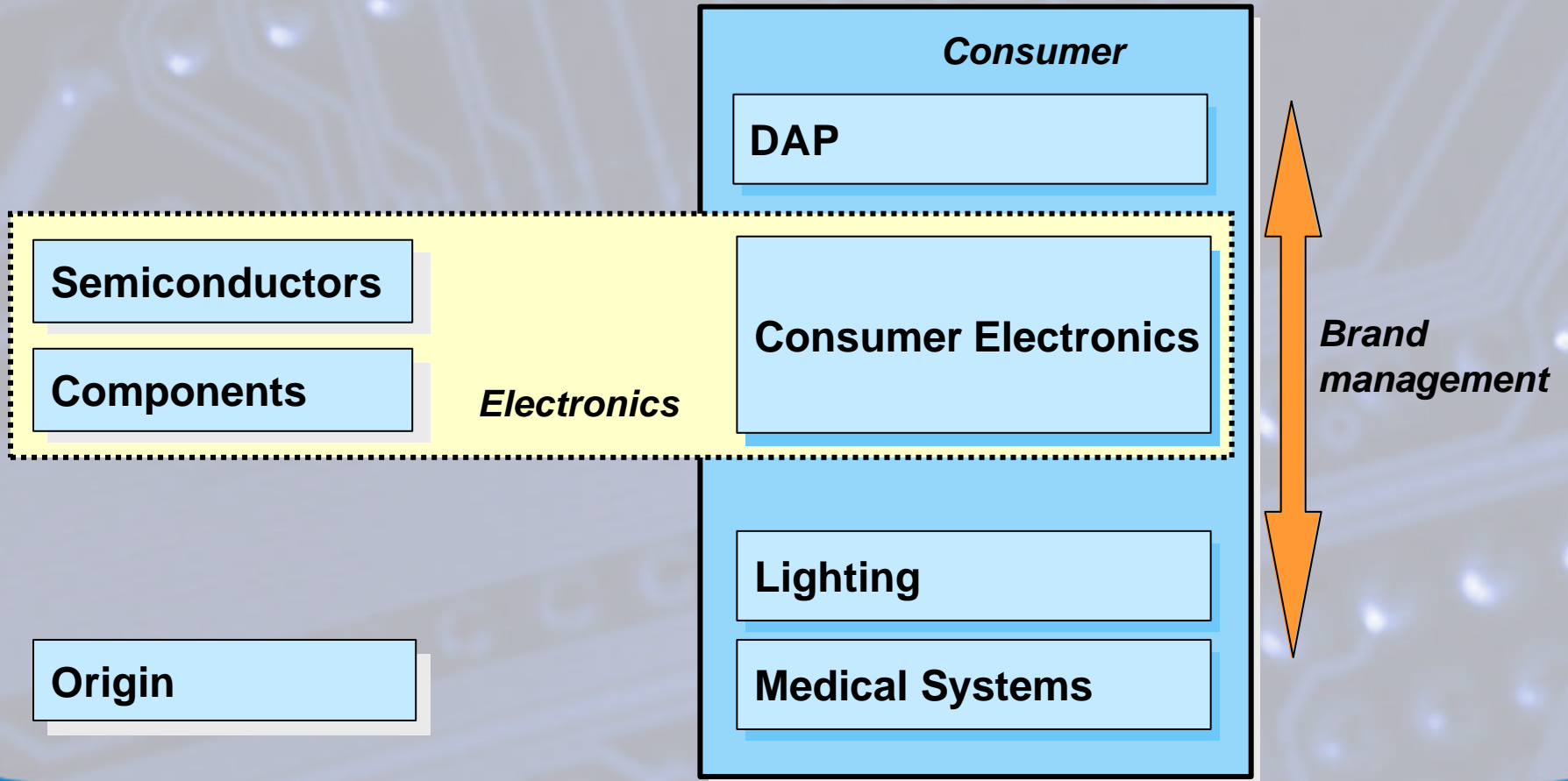
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Philips Semiconductors' position in Philips



Philips Semiconductors Sales & Support



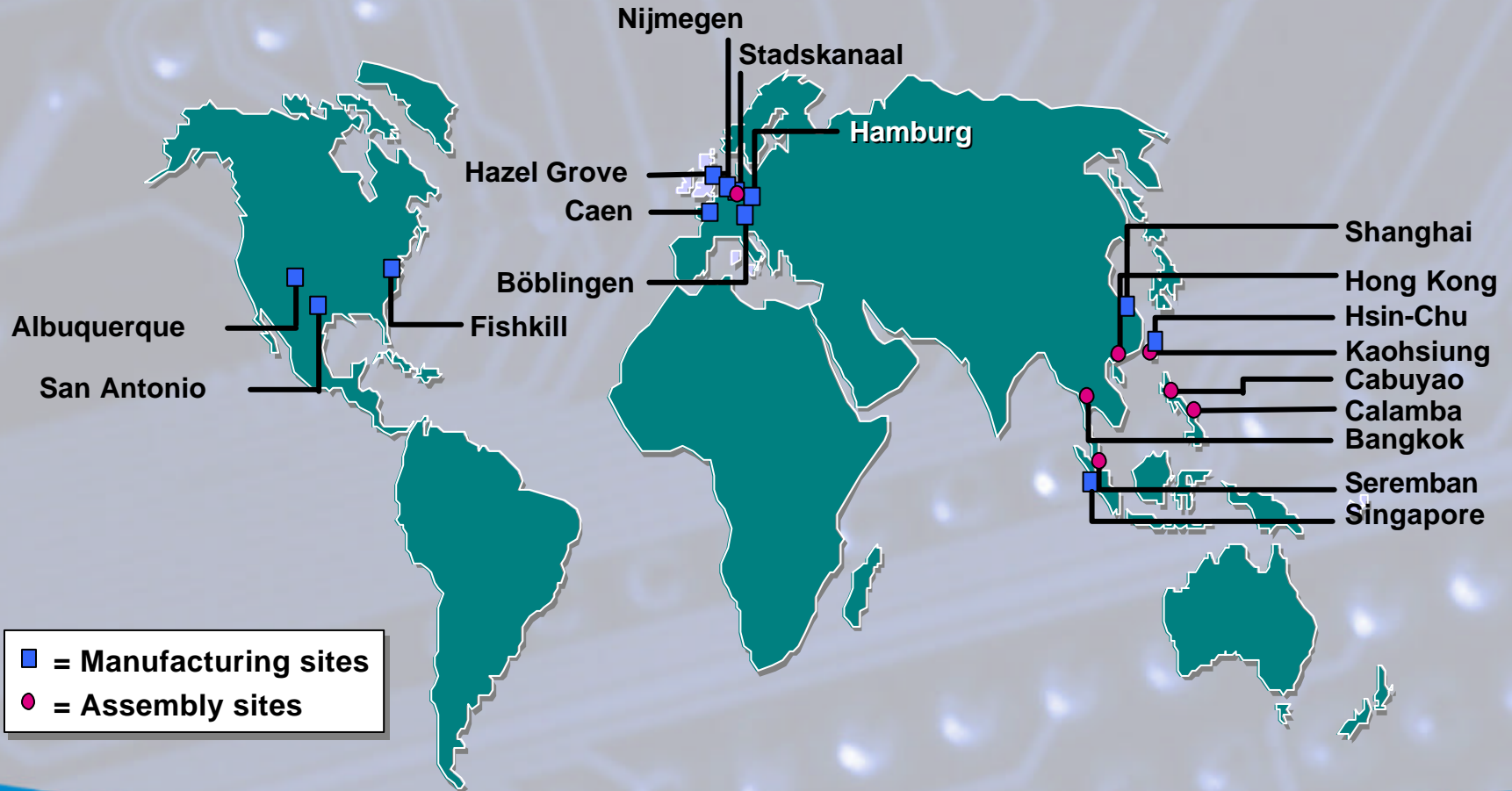
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Philips Semiconductors

Manufacturing and assembly sites



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1999 Final rankings - Top 20 Worldwide Total semiconductors (millions of US\$)

Company	1998 Rank	1999 Rank	1998 Revenue	1999 Revenue	Change %	99 Market Share %
Intel	1	1	22,784	26,806	17.7	15.9
NEC	2	2	7,947	9,210	15.9	5.5
Toshiba	4	3	5,913	7,618	28.8	4.5
Samsung	6	4	4,743	7,125	50.2	4.2
Texas Instruments	5	4	5,820	7,120	22.3	4.2
Motorola	3	6	7,088	6,394	-9.8	3.8
Hitachi	7	7	4,668	5,554	19.0	3.3
Infineon	10	8	3,909	5,223	33.6	3.1
ST Microelectronics	9	9	4,199	5,077	20.9	3.0
Philips	8	10	4,448	5,074	14.1	3.0
Hyundai MicroElectronics	22	11	1,799	4,830	168.5	2.9
Fujitsu	11	12	3,856	4,661	20.9	2.8
Mitsubishi	12	13	3,693	4,474	21.1	2.7
Lucent Technologies	14	14	3,202	3,780	18.1	2.2
IBM Microelectronics	13	15	3,234	3,520	8.8	2.1
Micron Technology	20	16	1,858	3,410	83.5	2.0
Matsushita	15	17	2,634	3,214	22.0	1.9
Advanced Micro Devices	16	18	2,543	2,870	12.9	1.7
Sharp	19	19	1,849	2,684	45.2	1.6
SANYO	17	20	2,195	2,552	16.3	1.5
Sub-total			98,382	121,196	23.2	71.9
Others			40,304	47,476	17.8	28.1
Total market			138,686	168,672	21.6	100.0

Source: Dataquest (March 2000)

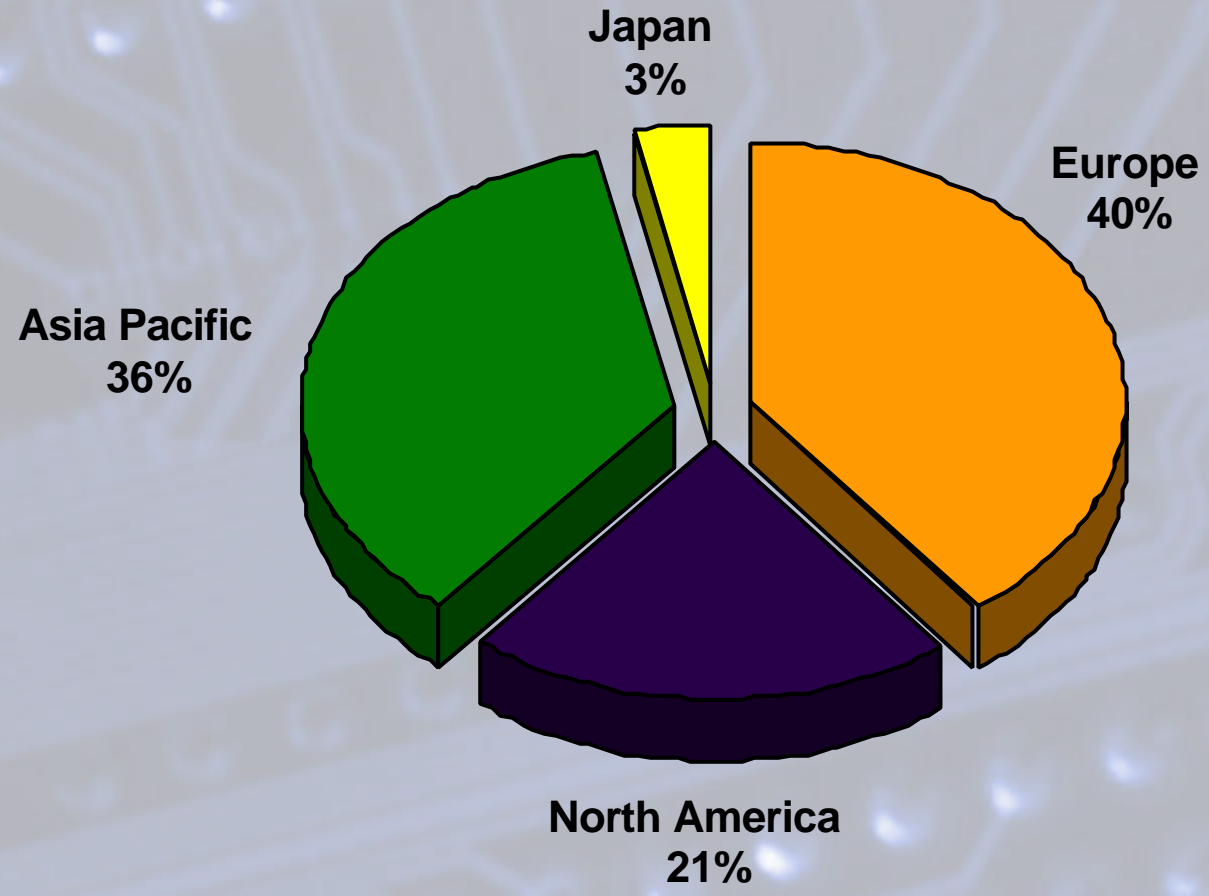
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Total sales 1999 by region

In percentages



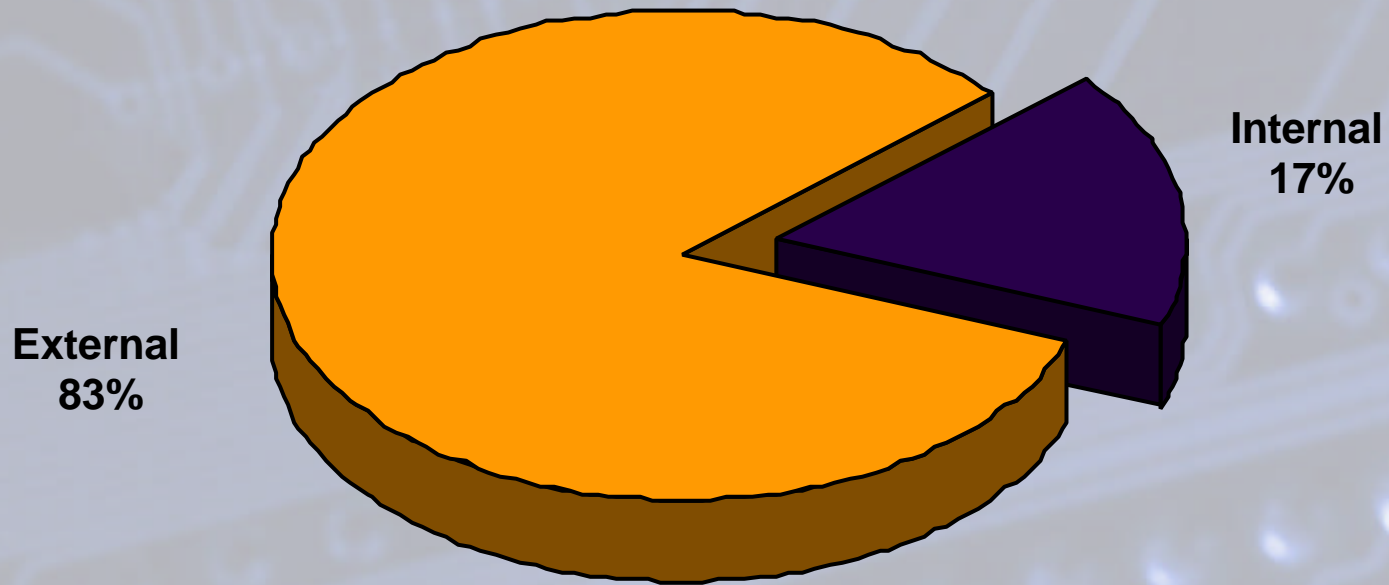
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Total internal vs. external sales 1999

In percentages



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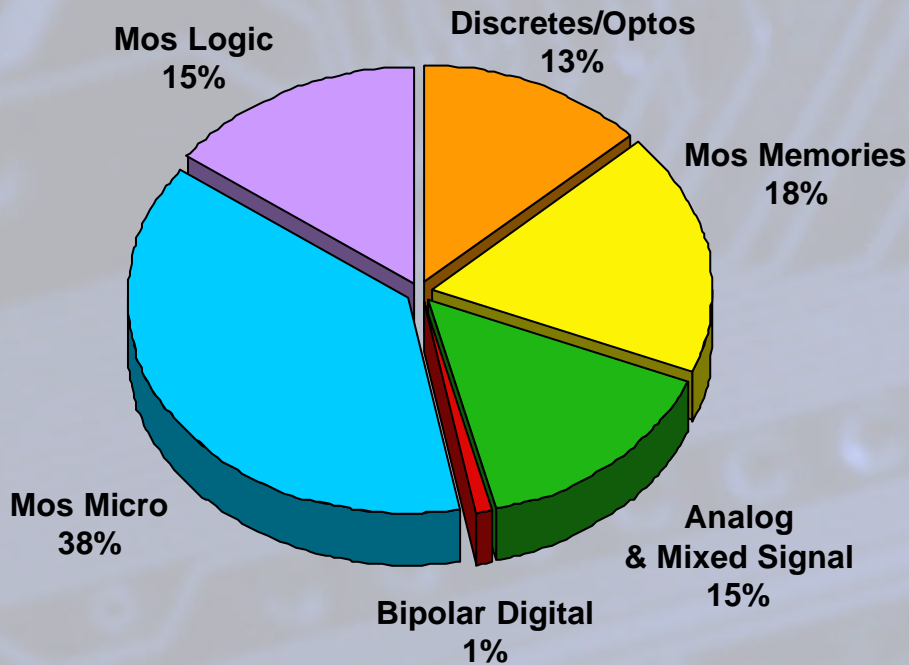


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Technology portfolio 1999

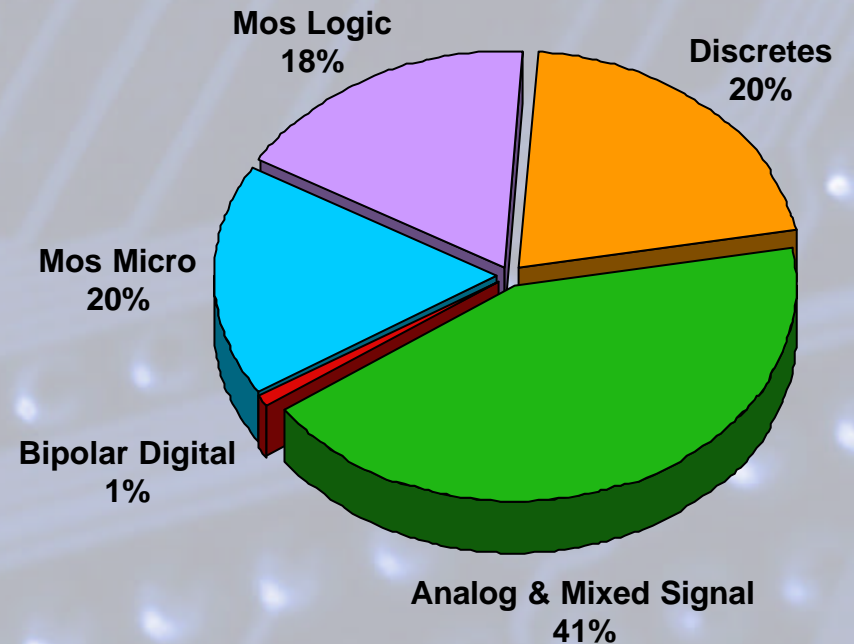
Compared with industry

Total Semiconductors Worldwide



Source: WSTS

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Philips Semiconductors

Key figures in M Euro

	1996	1997	1998	1999	2000 Q1
Sales to thirds	3536	3144	3212	3797	1225
Internal Sales	528	649	750	761	210
Total sales	3064	3793	3962	4558	1435
IFO	369	766	773	620	241
Headcount	25833	26916	26583	29952	30871

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Increasing investments in future growth

<i>Million Euro</i>	1996	1997	1998	1999	2000
Capex	552	340	411	646	1425
R&D	422	447	508	783	941

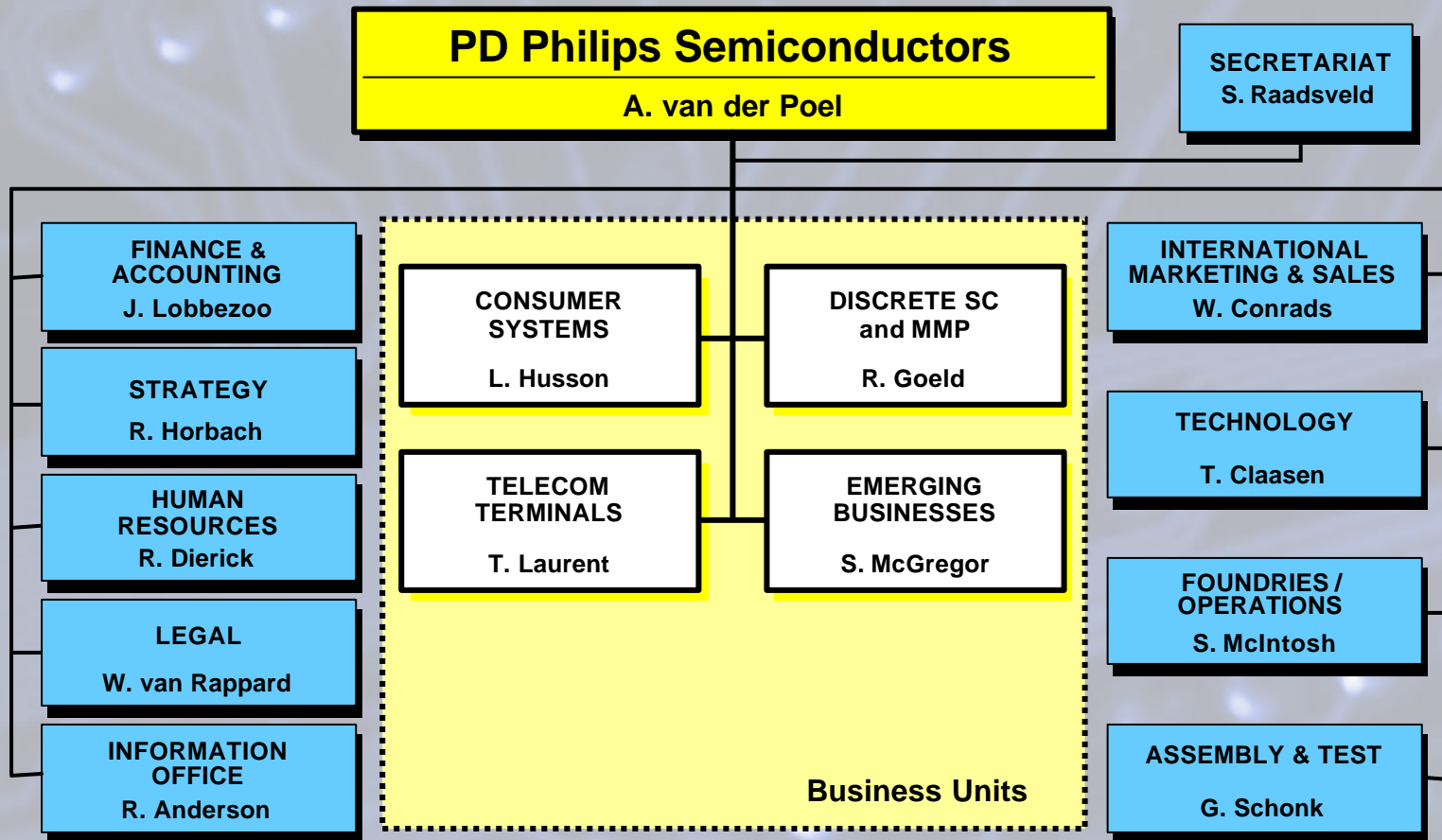
*excluding equity investments in new joint ventures and outsourcing

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Organization as per Sept 1st 2000



Philips Semiconductors

At a glance

- Major division of Philips Electronics, world's 8th largest electronics company
- World's 10th largest semiconductor supplier, sales around US\$ 5 billion in 1999
- 31,000 employees
- 18 manufacturing and assembly sites in 11 countries
- 4 System Labs and over 30 Design Centers
- Over 100 sales offices in more than 50 countries
- Over 45 years of semiconductor experience
- 26.5% shareholder in TSMC

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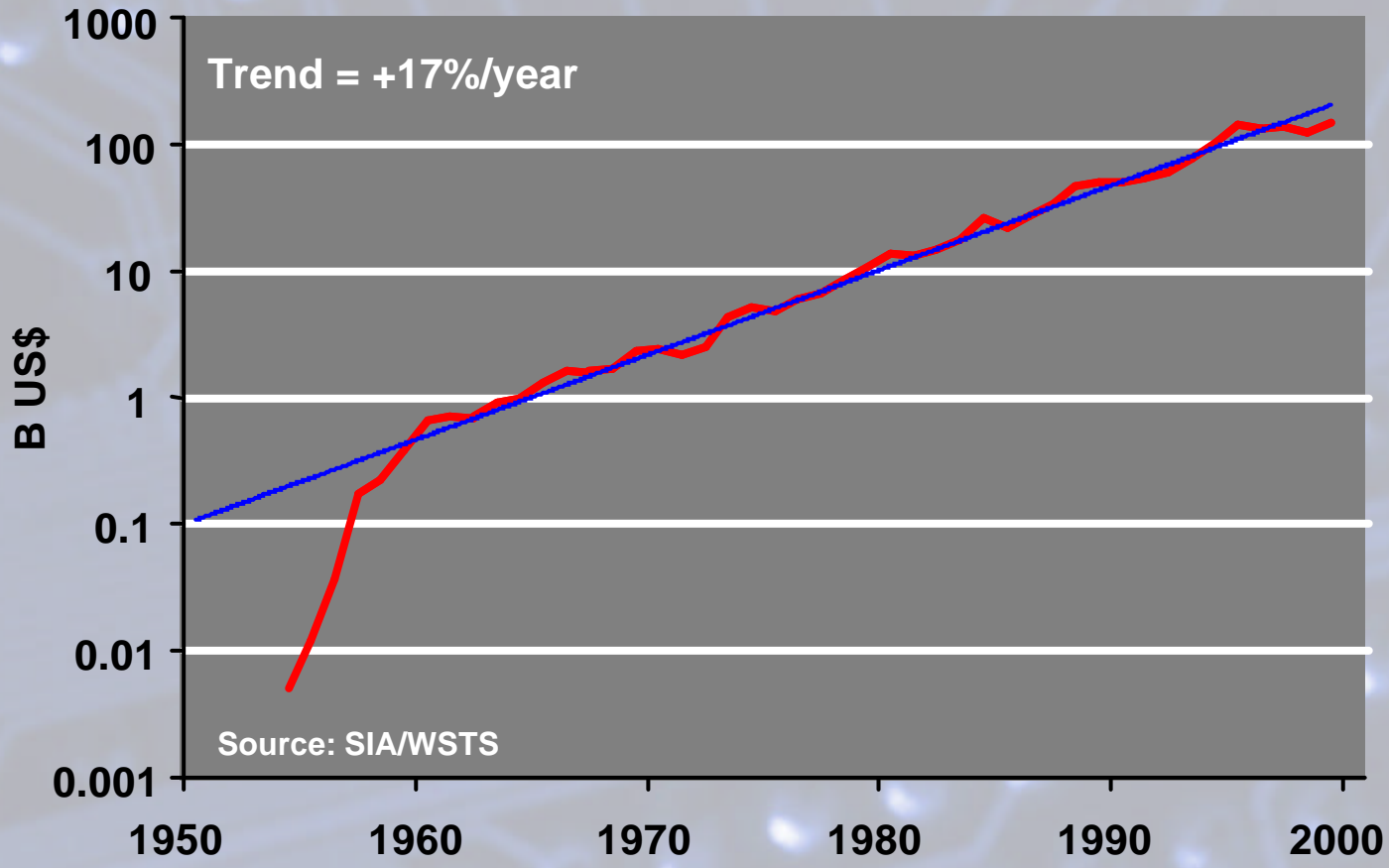
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50 years growth of world Semiconductor industry



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Market growth 2000

	Growth % 2000 versus 1999				
	Americas	Europe	Japan	APAC	World
Jan/April 2000 ytd	25.8	32.2	40.4	45.4	35.1
Forecast 2000 (total year)	24.4	31.7	30.9	37.2	30.6

Source: WSTS May 2000

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Main key competencies for future growth

- ***High-volume, low-cost manufacturing capabilities***
- ***Wireless:*** connectivity and interconnectivity for the home, office and on the move
- ***Flat Displays:*** drivers and display electronics
- ***Low power:*** process technologies and power-management expertise for mobile applications
- ***Mixed-signal processing:*** analog and digital signal on one chip (e.g. user interface speech technology)
- ***Secure access, Smartcard, Crypto:*** supporting our developments for the Web
- ***Speed:*** hardware and software platforms and ASIC capabilities for fast and flexible reaction

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Top 3 positions in key markets

Consumer

Signal processing in TV (1)
TV picture improvement (1)
Tuners (1)
Digital set-top boxes
Bluetooth
Optical storage/DVD

Communication

Wireless RF (1)
LCD drivers (1)
Wireless baseband
Battery management

PC/PC peripherals

Monitor deflection ICs (1)
Interconnectivity
Optical storage

Automotive

Car audio (1)
In-vehicle networks (1)
Car immobilizer (1)

General

Discretes
Identification (Smartcard)
CMOS Logic

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Philips Semiconductors and VLSI: *Rationale for the merger*

Philips Semiconductors:

- Adopt ASIC mindset and capabilities, which can accelerate our “Going Digital” ambitions
- Leverage cellular baseband business
- Strengthen our USA business
- Accelerate growth in Networking using ASIC technology

VLSI Technology:

- Create credibility for key customers; more critical mass
- Gain access to high-volume, low-cost manufacturing
- Access to key technologies and ability to invest in high-growth opportunities

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Philips Semiconductors and VLSI: *Strategic benefits*

- “Superpower” in wireless communication technologies
 - most complete wireless technology portfolio from a single source
 - poised for leadership in communications convergence market
 - ready for next-generation data-centric mobile communications products (Bluetooth wireless technology, GPRS)
- Impulse for other key technological areas like set-top boxes (STB) and networking
 - access to MIPS, HDTV capability
- Dovetailed ASIC methodologies:
 - VLSI Velocity[®] Rapid Silicon Prototyping (RSP)
 - Philips Nexperia[®] Silicon System Platform (SSP)
 - Together, a “system-specific Intellectual Property (IP) Platform”

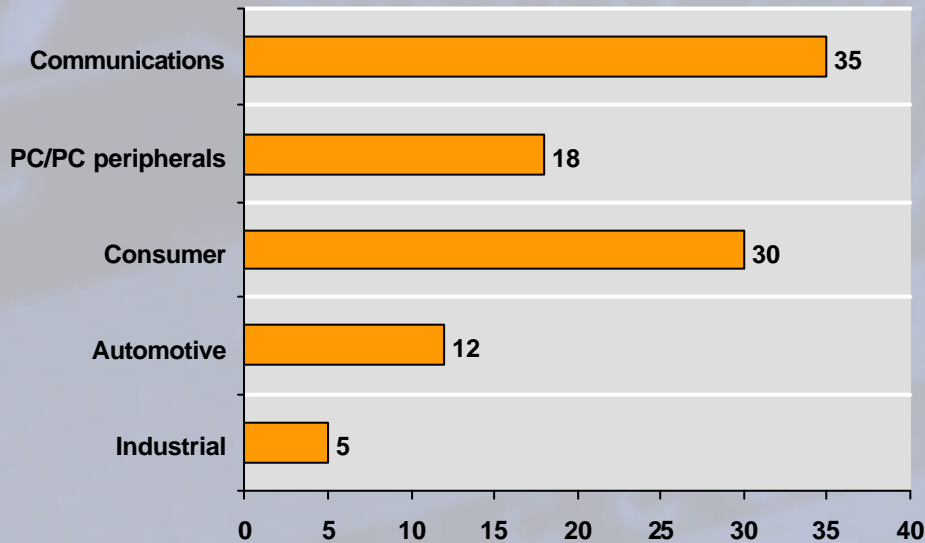
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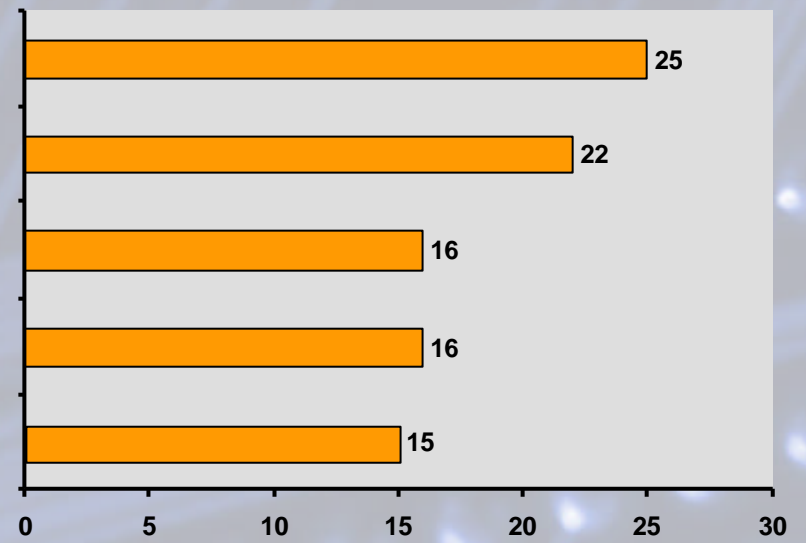
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Well-positioned in growth markets

**Philips OEM sales 1999
by market segment (%)**



**CAGR % growth 99-03
market by segment**



Source: Philips

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Focus on leading customers

***Over 50% of sales
with 25 key and strategic accounts***

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Top 3 customers per market segment 2000

Communication	Consumer	PC / PC Peripherals	Automotive	Distribution
Ericsson	Philips	Apple	GM	Arrow
Nokia	Sony	Philips	Ford	Avnet
Philips	Samsung	HP	DaimlerChrysler	WPI

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Technology

- R&D expenses 16%-17% of sales for:
- Process development:
 - CMOS development partnership with STM: in line with ITRS roadmap
 - World leader in QUBiC processes for RF applications
- Nexperia: Leader in reusable, programmable HW/SW platforms
 - Lower development costs for customers, easy customization and faster time to market
- Methodologies:
 - Rapid silicon prototyping: faster system/ product verification and faster time to market
- Innovation and research:
 - System development and new creative solutions

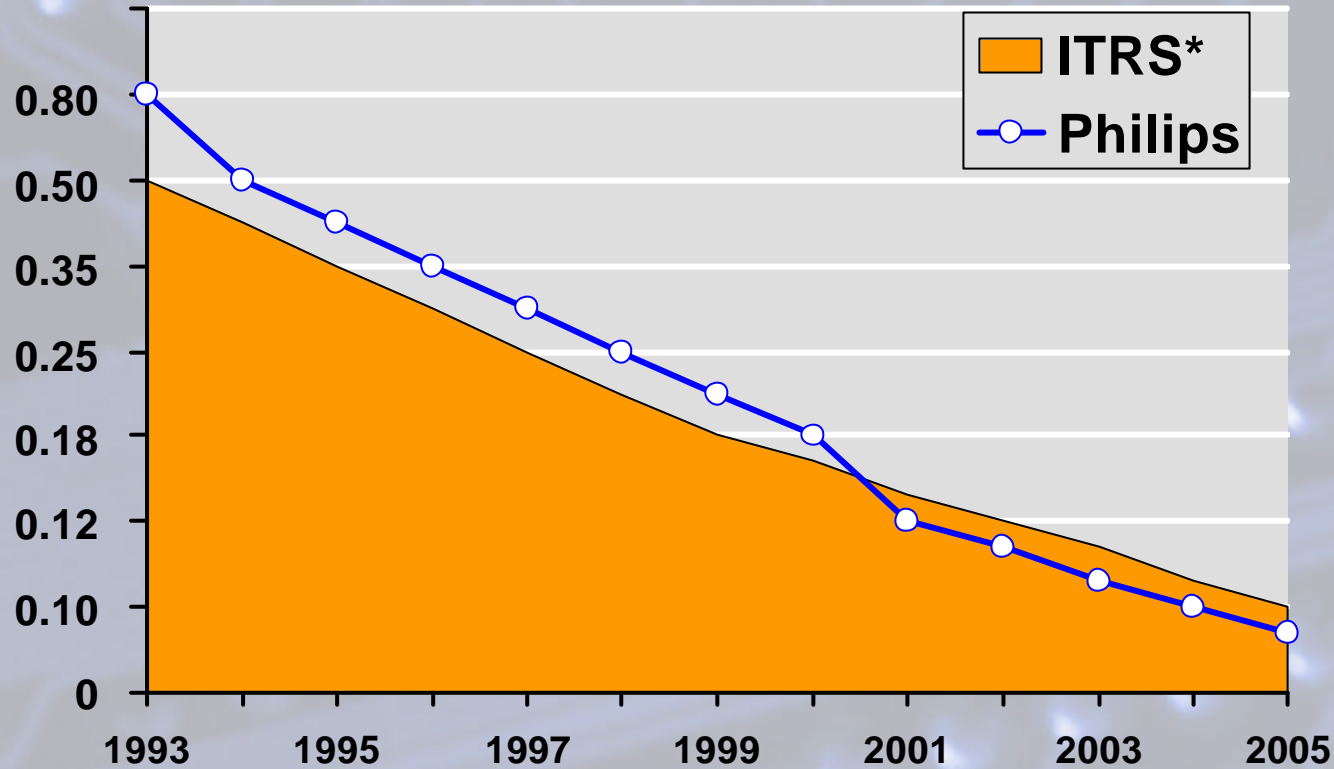
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Accelerating our technology roadmap in 2000 and 2001

Feature size in microns



* International Technology Roadmap for Semiconductors

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Leveraging partnerships and external consortia in all phases

- **STMicroelectronics**
- **TSMC**
- **SEMATECH**
- **IMEC**
- **Medea, strategic supplier programs**

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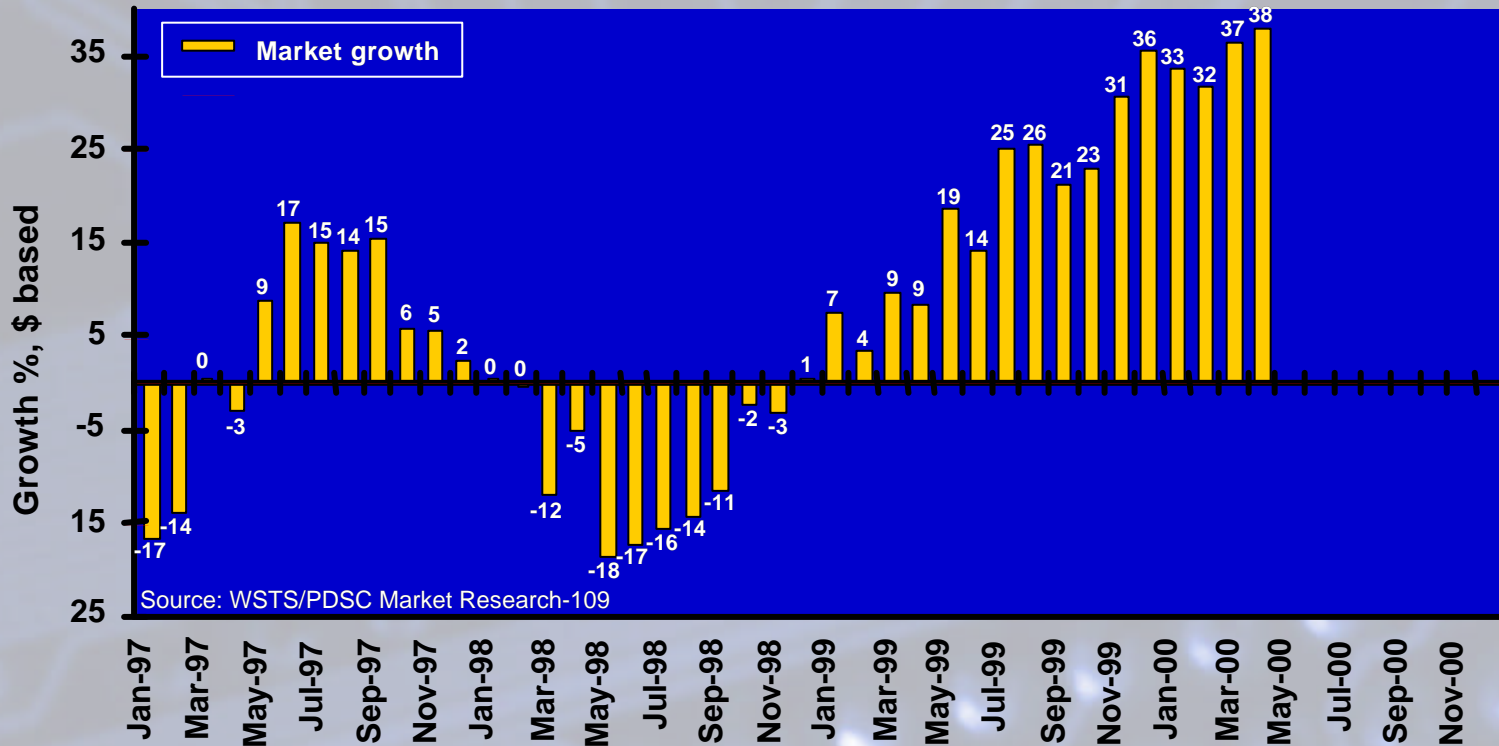
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Worldwide semiconductor growth rate (\$ based)

Growth in the month compared to same month previous year



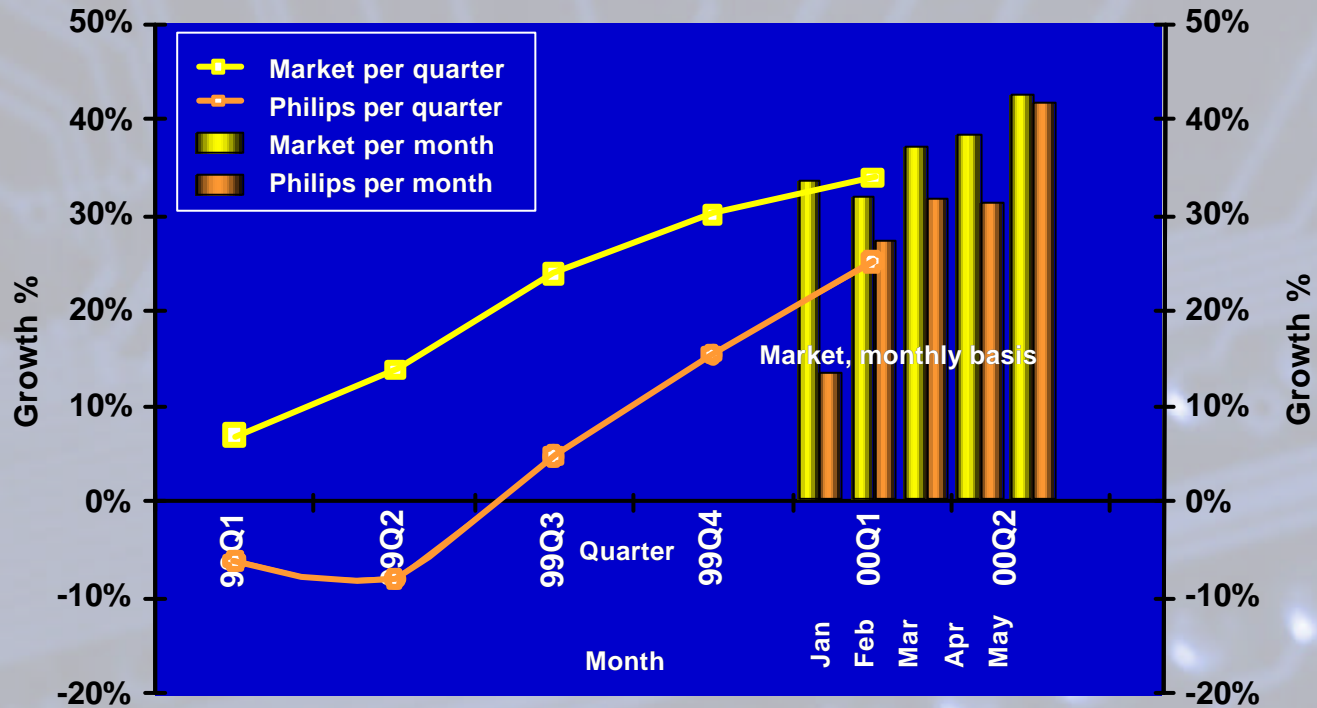
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Closing the growth gap

Market growth versus Philips sales growth (\$ base)



Source: Philips, WSTS
 1999 growth comparable to 1998, excl. VLSI
 2000 growth comparable to 1999, incl. VLSI

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Current status

- We're in the same ballpark (sales growth) as the industry now
- All time high sales and B/B ratio > 1.5 every month
- Order books triple the size of last year
- Shortages in the whole industry; in our case aggravated by the Albuquerque fire
- We moved scarce resources (people, wafers) from Mass Storage to more attractive markets
- We expect approx. 10% higher sales in Q2 than the 1435 million euro sales of Q1-2000 (over 50% more than Q2 1999)
- We will be capacity constrained throughout 2000

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Impact of the fire in Albuquerque

- Severe power down in State of New Mexico, March 18, 2000
- Fire in furnace cluster during power down
- Immediate loss of wafers: 7000
- Smoke and water damage: 13 days loss of production
- Back at pre-fire wafer start level by 2nd half of May
- Most severe impact on BiCMOS (QUBiC) products
- All in all, a loss of about 5-6 weeks

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New emphasis and new opportunities

- Our solid profitability is recognized
- We're catching up with industry growth rates
- VLSI acquisition offers tools, mindset and methodologies, but high-growth opportunities as well
- Trends in society and consumer behavior work in our favor
- Our ambitions are well supported by the Philips Electronics Board

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Main trends in society and consumer behavior

“Free and Easy”: Free to move, Easy-to-use

- Trends and requirements that were controversial or impossible are / will be normal
- Enabled by electronics
- Enabled by semiconductors
- Persistent and pervasive

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“Free to move, Easy-to-use”

- Freedom and individualism and ...
- Desire to stay connected (anywhere, any time)
- Blurring borderlines between work and leisure
- Convenience and ease of use
- The pervasive, often unconscious presence of electronics
- Increasing concerns for the environment (e.g. power)
- ...

In other words:

- Freedom to choose when to work, relax, communicate, anywhere, any time, making use of lightweight and easy-to-use equipment

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Consequences for Electronics Companies

- **Portable, Cordless, Wireless equipment**
- **Low power (on the move and in the home)**
- **User-friendly: simplicity outside, complexity inside**
- **Blurring boundaries: Voice and Data by phone, Internet access by PDA, Personalized TV**
- **Contact-less, secure, simple identification, authentication, authorization: payment, access**
- **Ability to meet (anticipate) yet undefined consumer demands**
- **Flexibility by “Standardization”: platforms**
- **Going beyond the old slogan “C & C” (Communications, Computers)**

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Which Semiconductor companies will be successful in this environment?

Those who build on the following principles:

- speed of access is more important than speed of processing
- low power is more important than high power
- fast and complex can be reconciled (re-use principles)
- future-proof and flexible concepts are enabled by general architectures and ASIC methodologies
- experts in cross leveraging will win over single application experts
- the more digital the world becomes, the more important analog expertise is
- (embedded) software must enable ease of use

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VoIP

Bluetooth

i-code

Greenchip

Nexperia

802.11

Sea of IP

QUBIC

RF

CoReUse

DVP

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Vision

- **We foresee a substantial change in our industry and the markets in which our customers are active**
- **Networked products for the home, for the car or for people on the move enable new, IP (Internet Protocol)-based services and experiences**
- **The most successful companies will no longer be experts in separate markets, but will be masters of cross fertilization**

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Vision

In this environment of networked applications we aim to be:

- **Leader in connected and interconnected systems in the home, on the move and in the car**
- **Customers' first choice in Audio, Video, Communication terminals, and their combinations**
- **Leader in standard ICs and discrete semiconductors**
- **A leading supplier of complete, cost-effective, and easy-to-use systems-on-silicon**

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Ambition level

We aim to achieve a 10 billion euro sales level,
run rate, by the end of 2002

- Under the assumption that the market outlook remains positive

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Building on earlier strategy

- **Market-specific and multi-market products are both attractive**
- **Subcontracting, Partnerships, Participations (TSMC, STM, TriMedia, foundries, assembly/test)**
- **Platform and architecture strategy**
- **Design and reuse methodologies, accelerated by VLSI acquisition**
- **Focus on Key accounts, Distribution and EMS-providers**
- **Invest for growth, maintaining no-nonsense cost and asset management**

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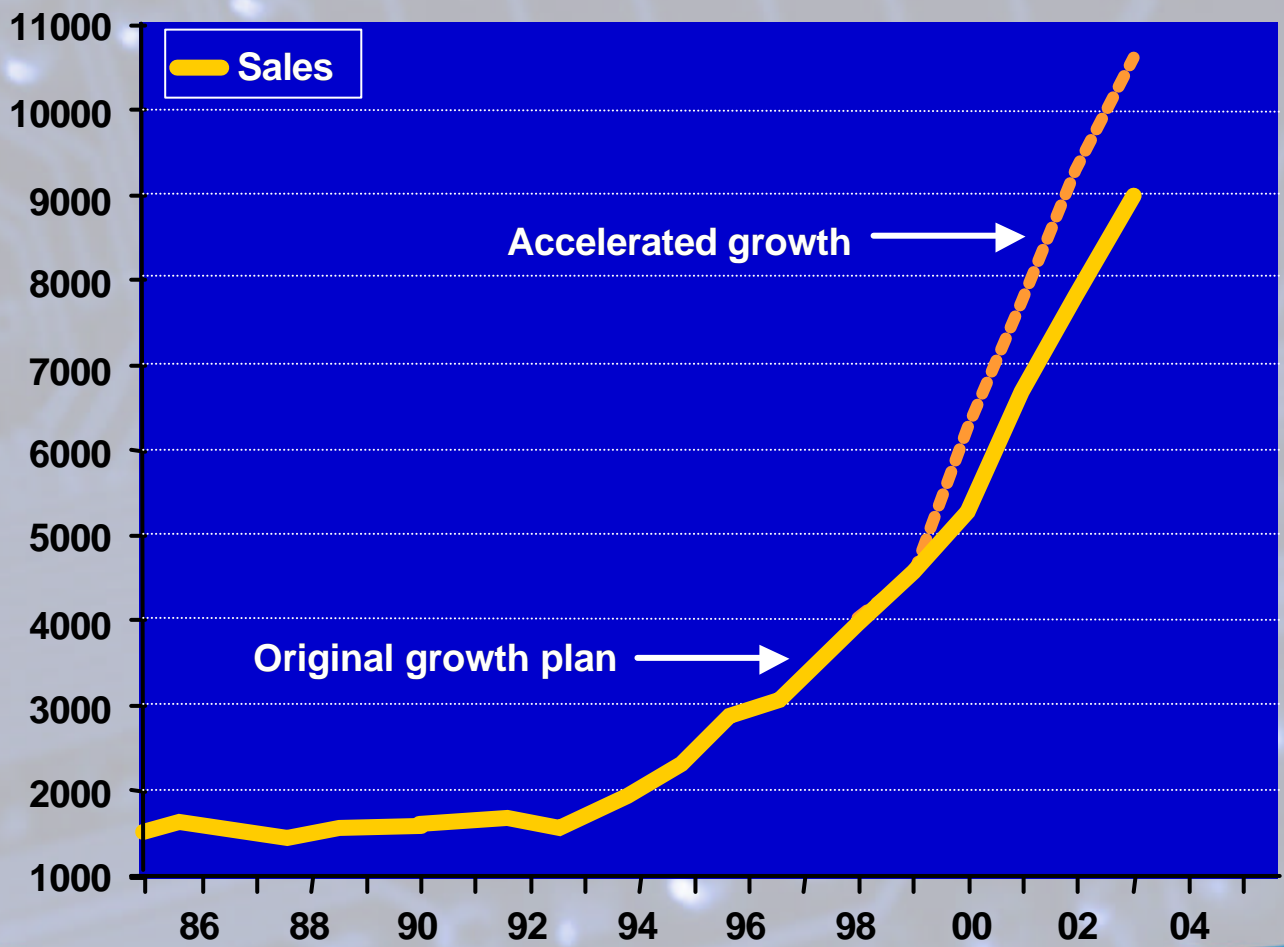
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Sales growth 1985-2003 (in B Euro)



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Focus on Growth:

The four cornerstones

- **Portfolio: a solid mix of high-growth opportunities, such as Communication, Networking, Digital Consumer and cash-rich businesses**
- **Pro-active investments in Capital Expenditures and R&D**
- **Tools, processes, platforms, intellectual property rights (IPR)**
- **Mindset, organization, ways of working**

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Investments in growth: *Capex and R&D*

- We spent 650 M Euro capital expenditures (capex) in 1999
- In 2000 we will spend approx. 1.7 billion euros (including the acquisition of the MiCRUS fab)
- Including SSMC we invest the equivalent of 2 billion euros
- While we continue to outsource about 20% of wafer demand
- About 30% of capex is for assembly and test
- Joint investment remains the preferred model for large facilities (such as SSMC, 300mm pilot fab with ST)
- R&D investment, weighted average of 4%-5 % for Discrete Semiconductors and 18%-20% for ICs
- Partnerships and participations for niche technologies

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Acquisition of MiCRUS fab

- Currently a 0.35 / 0.25 micron CMOS fab in East Fishkill, NY
- Acquisition from IBM (July 2000) and renamed Philips Semiconductors Fishkill
- Capacity approx. 20,000 8-inch wafers per month
- Wafer supply arrangement with IBM for 2001-2002
- CMOS supplies for Philips as of Q4-2000
- QUBiC supplies scheduled as of Q2-2001
- Non-volatile CMOS technologies to be installed
- Main purpose is to achieve second source for advanced BiCMOS technologies (QUBiC-3 and QUBiC-4)

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Market growth

Expectation of WSTS and SIA per May 2000

	2000 B \$	2000 %	2001 %	2002 %	2003 %	CAGR % 99-03
WSTS view	195	31	20	14	9	18
SIA view	195	31	25	14	12	20

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Market Outlook:

Summary

- The markets that we serve, grow as fast as the worldwide TAM
- Market downturn expected not earlier than late 2002
- Healthy CAGR 1999-2003

- Starting in H2 2000 and subsequently in the years ahead, we expect to meet or beat the market, because of
 - the increasing importance of Telecom in our portfolio
 - growth potential of the (for us) Emerging Businesses
 - the mutual strengthening of Philips and VLSI
 - our “cross-leveraging” capabilities
 - our investments in Digital Consumer
 - our positioning and investments in Discretes

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Reasons for Industry Consolidation

- **Level of manufacturing investments**
- **Level of R&D investments**
- **Profitability**
- **Cyclical**
- **Commitment level of parent companies**

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The industry in 2005

- **Small group of very large players**
- **Sub-top of large players**
- **Small number of large, pure-play foundries**
- **Shrinking group of medium-sized companies, caught in the middle**
- **Large group of niche players**

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In conclusion

- We are at par with the industry growth today
- We are well-positioned for the growth markets
- The market environment supports our ambition to achieve a 10 billion euro run rate sales level by the end of 2002

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