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ISSUER COMMENT

27 April 2022



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RATINGS

Royal Philips N.V

LT Issuer Rating	Baa1
Outlook	Stable

Source: Moody's Investors Service

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Royal Philips N.V.

Poor Q1 results broadly as expected, rating is weakly positioned

On 25 April 2022, [Royal Philips N.V.](#) (Philips, Baa1 stable) published a weak set of Q1 results including group sales down 4% versus last year due to supply chain challenges and disruption from the Respironics field action (repair and replace program on some of the company's respiratory devices), a significant decline of its adjusted EBITA margin as a result of the sales decline and cost inflation. The cash on balance decreased to €1.4 billion (8% of group sales) end of March 2022 from €2.3 billion in December 2021. The Q1 results are credit negative but the Baa1 rating with a stable outlook remains unchanged based on our expectation that the company's operating performance and its credit metrics will improve during the next quarters.

The adverse sales performance was expected since the company guided in January 2022 for a high single digit decline in Q1. Despite a highly uncertain environment amid supply chain disruptions, inflationary pressures, Ukraine-Russia crisis and lockdown in China, the company confirmed its guidance - initially published in January 2022 - for the full year that includes a recovery of the operating performance in the second half of the year and overall 3-5% sales growth and margin improvement for 2022. Philips believes that it can mitigate cost inflation by price increases to be progressively passed on to customers and tight cost control.

The company announced that the provision covering the costs from the recall field action (costs to repair and replace the faulty devices and communicate with customers) will further increase by another €165 million from €719 million according to the latest estimate communicated in January, a credit negative. The full provision, as it stands today is four times higher than the €250 million provision the company initially estimated in April 2021 when this issue first arose. Following the trend over the past 12 months, we think there is a risk that this provision could increase further, a credit negative. This highlights Philips' mixed track record in terms of product quality, a credit weakness.

Philips' rating transitioned from well to weakly positioned during the course of 2021. Given Philips' current strong order book, we expect that revenue growth will return as supply chain challenges gradually ease likely in the second half of 2022 driving an improvement in credit metrics and hence supporting the rating. However, a scenario where significant additional costs from the recall field action or litigations would arise, combined with weaker than currently expected operating performance and more aggressive debt-funded M&A or shareholder distribution, could lead to downward rating pressure.

Moody's related publications

[Royal Philips N.V. - Update to credit analysis, 3 March 2022](#)

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REPORT NUMBER

1327208

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