FINAL TRANSCRIPT

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PHG - Q3 2006 Royal Philips Electronics Earnings Conference Call

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PRESENTATION

Operator

Welcome to the Royal Philips Electronics Third Quarter Results call on Monday October 16, 2006 for the introduction by Mr. Pierre-Jean Sivignon, Chief Financial Officer of Royal Philips Electronics. [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 - EVP and CFO*

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

The largest single item in our results this quarter is the EUR4.2 billion result from discontinued operations. This relates to the disposal of our Semiconductor division and the figure contains many items for which we have given you a specification in the press release. You will also see in our balance sheet that the expected large amount of cash has been received. It brings the Semiconductor disposal to a conclusion in such a short period of time and we see this as a tribute to the very many people in Philips and I would like to publicly recognize this today.

Before getting into the details of the results I would like to explain the change in the accrual for asbestos claims against a [subsidiary] company. Up until now the [subsidiary] has accrued for asserted claims as and when they were received and we have fully disclosed the situation in our annual reports over the last [two] years. An accrual with respect to unasserted potential future asbestos related claims had not established in prior periods since the company, with the assistance of an independent asbestos evaluation experts concluded it could reasonably estimate the liability in accordance with applicable accounting rules.

In the third quarter, in light of additional claims history experienced by the [subsidiary] and other change of circumstances, the third party experts provided the company with a projection of the [subsidiary's] liability for pending and unasserted future asbestos related claims up to 2016. Accordingly the [subsidiary] recorded an accrual for the additional liability.

Additionally the anticipated insurance recoveries from insurance carriers with which agreements have been reached were recognized. This has resulted in a net pretax charge in this quarter of EUR265 million. This quarter has again been one in which we have seen more evidence of sales growth and increasing profitability towards our margin targets. Let me be more specific. The comparable growth for the company was an excellent 5% with all divisions except consumer electronics being above this figure. In fact Medical was 6%; DAP was 9% and lighting was 10%; the average for those three divisions being 8%. This means that we are growing in the right areas.

These growth levels support our average annual target of 5 to 6%. The EBIT in the quarter was EUR290 million before allowing for a provision of EUR265 million relating to the change in accounting treatment for asbestos claims. Excluding this amount, EBIT was 4.6% of sales and compared with 3.5% of sales in 2005 once excluding the gain of EUR136 million on the TPV transaction which took place in the third quarter of 2005. The underlying margin in this quarter was in fact higher than 4.6% as it included some charges that we have specified in the press release. This improvement helps us move to the higher levels of margin that we have been forecasting. Please remember that the fourth quarter is always our biggest.

In Medical Systems the comparable growth was 6% which is in line with our annual target of 6% but it looks like 2006 will be higher. The 6% growth in equipment order intake gives us a growth of approximately 9% for the first three quarters of this year. In addition the order intake for iSite PACS was excellent so we are far exceeding there the plans that were formed at the time of the acquisition of Stentor last year.

The margin in the quarter compared to one year ago increased in both absolute amount and percentage as we had forecasted. This improved performance was broadly based and evident in virtually all business units of Medical. In DAP the excellent quarter has given us a 9% comparable growth which again more than supports our annual target of 7%. This very strong growth came mainly in Shaving & Beauty and Oral Healthcare and was primarily focused in emerging markets, mainly China and Latin America. We included one month of AVENT which was in line with our expectations.

The underlying developments of the margin was strong and supports our annual EBIT target of 15 to 16% prior to purchase accounting charges. We continue to work towards taking cost out of this division to liberate funds for investment in innovation and marketing. Sales in Consumer Electronics on a comparable basis declined by 1%. There was however continuing growth in Connected Displays and Peripherals & Accessories. The margin in the quarter was 2.2% which is higher than what we recorded in the second quarter. This positive margin development in spite of the difficult market circumstances at the beginning of the quarter is a tribute to the robustness of the business model and to our focus on margin improvement.

The lack in sales growth was 10% driven up by UHP, Automotive, Special Lighting and Lighting Electronics and supports our annual target of 6%. Lumiled is on track to achieve 25% annual sales growth. The Lighting margin was strong after allowing for charges taken in the quarter that we have specified for you in the press release.

In other activities we continue to work towards the disposal of the businesses and we have continued to make progress. I expect we will make further announcements soon. The EBIT includes the EUR265 million charge that we have taken in relation to asbestos liabilities.

In unallocated we continue to have costs to become SOx compliant but these costs will not continue after the end of this year. The net cash in the quarter was 3.4 billion compared to EUR2 billion net debt at the end of the second quarter. This change was totally due to the receipt of the proceeds from the sale off shares in our former Semiconductor division.

During this quarter we have implemented a share buyback program that we announced three months ago. During the quarter we bought back 32.4 million shares at a cost of EUR848 million which is at an accelerated rate as we indicated on September 11. The inventory percentage of 12.7% is 20 basis points lower than one year ago and we consider this as a strong performance. There are still one or two areas where the inventory to sales ratio can be improved and we are working on those areas. The results from non-consolidated companies reflect the lower results of LG Philips LCD which were anticipated.

There are some items that you must take into account when forecasting the results for the fourth quarter. The main ones are; in Medical we are making the assumption that the Intermagnetics transaction will close in Q4 which will create a charge in the quarter of approximately EUR75 million. Due to the changed standing pattern of the brand campaign we expect Q4 to include an amount of EUR85 million. The fourth quarter of 2005 included EUR187 million release of a post retirement provision for Medical benefits and this would not be repeated in the fourth quarter 2006. Excluding the expected Intermagnetic charge of EUR75 million and the Q4 2005 accrual for MedQuist we expect the Medical margin in Q4, in amount and in percentage, to be above last year. And I would like now to open the call for your questions.

QUESTIONS AND ANSWERS

Operator

Thank you sir. [OPERATOR INSTRUCTIONS]. The first question comes from Nicolas Gaudois from Deutsche Bank. Please go ahead with your question.

Nicolas Gaudois - *Deutsche Bank - Analyst*

Yes, hi there Pierre-Jean, just first question on the Group margins now that we are excluding obviously Semiconductor, would you care to help us model EBIT margins for our Group going forward versus your prior gain and it's including Semi of 7 to 10%? And I've got a follow-up on Consumer Electronics. Thank you.

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

Okay for 2006 I would say no change; we basically had guided you specifically product division by product division. I think those percentages, there is no change. And I would say that as far as the overall guidance of getting the Group, including Semiconductor pro-forma now in the range of getting to the 7% for next year, that guidance is confirmed.

Now I think as far as Unallocated and Other, we've guided you as closely as we could in the press release and if we need to do more I'm sure that Alan can do that offline. So I think for '06 we've been as precise as we can.

As far as '07 is concerned, we haven't made our decision yet and I think that we will be updating you on this at the beginning of 2007.

Nicolas Gaudois - *Deutsche Bank - Analyst*

Okay fair enough and on Consumer Electronics, specifically which is probably the guidance which is missing from the press release and your statement opening the call, your previous statement was just shy of 4 to 4.5% margin in '06, could you care to clarify this for this year and maybe give us a broader view on how margins would level up there? Thank you.

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

Yes I think on Consumer Electronics there is no change, I think the slight -- the slightly shy of the 4% which we had debated at the end of Q2 still holds. If anything the third quarter stripped off the incidentals is actually in progress, actually the -- so the total year we standby the number which should be sometime, something between 3.5 and 4% for the year. And our guidance for next year, as I said, hasn't changed, it will be in that domain. I think, as I said, I will come back to you in three months from now, but it shouldn't be very different from this. There is no change on Consumer Electronics, we'll continue to focus on margin and not guide you on revenue. No change there.

Nicolas Gaudois - *Deutsche Bank - Analyst*

Okay, thank you very much.

Operator

The next question comes from Mr. Janardan Menon from Dresdner. Please go ahead with your question.

Janardan Menon - *Dresdner - Analyst*

Yes, just a couple of questions, one is on your Consumer Healthcare Solutions business, what is the kind of outlook in terms of profitability and growth that we can expect over time? You're currently loss making to a small extent, is that likely to change over the profit in the coming quarters?

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

No I think on that particular line we have not guided you. It's a line where we basically have our investment, it's basically including two things, it's including Lifeline, right which is in reality positive and if you include the investments that we are doing in the other territories on that line, we are, this particular quarter on the slightly negative. We have not decided on guidance for next year, I think on this particular one we'll discuss it on the back of the Q4 numbers, but we're not expecting to be significantly in the black, I'm sorry, in the red there. We will guide you in three months there, but again, as I said, it's a combination of Lifeline which is a positive and some negative on the back of the investment we're doing in that particular territory.

DAP numbers, net of that, that is 15 to 16% as we've said a couple of times.

Janardan Menon - *Dresdner - Analyst*

Okay. And just going back once more to the Consumer Electronics. Given that you are pruning your sales quite a bit, can you give us some clarification as to what areas you're pruning these sales in? And to that extent, as you go through that process is there any upside that you can go back to your original 4 to 4.5% target rather than the 3.5 to 4?

And secondly, can you give us a number for the royalties for the quarter?

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

Okay. I think that we -- if you refer to the pruning of, by the sale or the disposal of Mobile which we actually announced a couple of a days ago, yes this will have a slightly positive impact on the mix. So I think your remark is absolutely correct, should that help us to go back to the 4 to 4.5 for next year, yes there is a positive impact there. As I said, I will come back to you early next year with that specific answer, but that definitely will help us.

In terms of more pruning, we try to increase Peripherals and Accessories via internal and external growth and that is as well adding to some accretion to Consumer Electronics. And in all the particular product group of Consumer Electronics we apply the model for profitability gain, if and when, including if and when it is at the expense of the revenue. So I wouldn't -- we're not planning any more pruning besides the phones, the phones was becoming very marginal for us, we had a world market share of around 3%, so for us that was becoming not very efficient. But the existing portfolio we have right now is the one we want to focus on and continue to improve in every sector and every piece of geography.

Janardan Menon - *Dresdner - Analyst*

And your statement that, as anticipated growth in [flat panel] showed signs of deceleration, can you just sort of clarify that comment? What kind of deceleration are you seeing?

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

Well there you remember that this is on the back of a very strong second quarter which was, there was a very high level of expectation because of the World Cup, in particular in the early part of Q2. So obviously the market knew that Q3 would be a bit of a slowdown in that particular domain. In all case I have to say that for Connected Displays which includes that particular LCD offering did actually well, and the reason why we did well is because we ended up, if you remember, the second quarter with an inventory which was under control. So if you talk about the market there was an anticipated slowing down of the market, if you talk about Philips, two things, a) we tried to isolate ourselves as much as possible from revenue to guide you on margin, and b) we finished Q2 with an inventory under control which enabled us to have a Q3 where year-on-year for Connected Displays actually improved compared to the year before.

Janardan Menon - *Dresdner - Analyst*

Okay thank you very much.

Operator

The next question comes from Mr. Navdeep Sheera from Lehman Brothers. Please go ahead with your question.

Navdeep Sheera - *Lehman Brothers - Analyst*

Thank you very much, good morning Pierre-Jean.

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

Good morning.

Navdeep Sheera - *Lehman Brothers - Analyst*

First question with regarding to Lighting, as I read it, the charges that you took in the quarter were one-offs, so the question is do we expect the division to go back to normal EBIT margins, so above the 12% for the year by the time we come to the fourth quarter? Thank you.

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

No actually we had indeed, I would say a rather high level of one-offs in Q3 which were basically related to some restructuring as well as some other one-offs including some write off of assets. I would consider that as a high level of one-offs and that doesn't change our guidance of Lighting where excluding the one-off, which again should be lower next month, would be an improvement year-on-year. So there is nothing changed on the guidance of Lighting compared to what we told you in particular at the analyst conference a couple of weeks ago.

Navdeep Sheera - *Lehman Brothers - Analyst*

Thank you for that. And secondly on Medical, are you still seeing the same level of top line seasonality going into the fourth quarter, so you see a sharp spike in sales, or has that lessoned this time around?

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

Well the answer is, it's always difficult to say. I think that we basically have guided you for the year on a revenue increase like-for-like of Medical of 6%, that's actually what we did in Q3. We expect to be slightly north of that actually for the year, this is, if you do the maths, you will see that that includes a Q4 which will be still high. Would we like to go away from that seasonality? Definitely yes because I think that would be probably better for the business. The reality of it though is that a lot of those budgets in those hospitals is awarded on a yearly basis and you have still very often the need to spend the money at the year end. So we're doing our best to avoid that seasonality, but it's turning out to be difficult.

So I would say that we are still expecting a strong, in comparative terms versus the other three quarters, a strong fourth quarter with a year which will be all in like-for-like north of 6%. But we will continue in the future to try to go away from the seasonality, but it's not easy. After having looked at it carefully, that's not an easy target.

Navdeep Sheera - *Lehman Brothers - Analyst*

Thank you for that Pierre-Jean, my final thing then I'll disappear. Judging by GE's results on Friday, you seem to be more optimistic going forward for Medical. Can I read into that market share increases which you could possibly with us? Thank you.

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

Well you know it's a bit early to fully read all what has been given in the past couple of hours, even say days on the back of Q3. I take some comfort from our incoming orders of Q3, because that's really what you should look at. I think 6% of incoming orders in the market which we know is the market which really grows at 4 to 5%, I would take some comfort from that. You remember that we had had a lower quarter in incoming orders in Q2, which obviously had raised a couple of questions, so we're back to 6% on Q3. Are we gaining market share? I think the market grows at 4 to 5, we booked orders at 6 so in my book that must mean that, yes, we must be doing well.

Navdeep Sheera - *Lehman Brothers - Analyst*

Thank you very much.

Operator

The next question comes from Mr. Jonathan Crossfield from Merrill Lynch. Please go ahead with your question.

Jonathan Crossfield - *Merrill Lynch - Analyst*

Yes good morning. My first question would be on the Other Activities where I guess following further divestments that you hinted to in Q4 and potentially lower future asbestos charges following this provision, how do you see the run rate of losses in that area developing over the next year or two?

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

Well basically in Other Activities if you look at the past three years as an average even though it had a declining impact during those last three years the asbestos charge was about, as an average 40 million all in. But with a declining effect actually coming down from three years ago to 2005 that kind of average impacted us over the first two quarters of '06. So I would say that, that kind of amount will [grow] away from the line Other next year.

In terms of the corporate investment portfolio which is still costing us money this year, in terms of operating margin and excluding the impact of divestiture one-offs I would say that next year we should be close to breakeven on that particular line. And we should be left with essentially a central research as well as or incubators and a couple of other incidentals. So I think next year you should have central research incubators and I would say a couple of incidentals like real estate gains which are very hard to produce and no loss on the back of asbestos and no more loss on the back of corporate investment. I think that's the guidance I can give to you for Other next year.

Jonathan Crossfield - *Merrill Lynch - Analyst*

Okay that's very helpful. Just as another quick follow-up. Do you have anything you can say about plans for the brand campaign going into 2007? Whether directionally it will be higher or maybe a little lower than we saw in 2006?

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

Well first of all we've guided you on the 2006 Q4, you saw that in Q2 we didn't catch up on the lag we had in Q2 versus the year before. So we guided you on Q4. It's too early to talk about next year, we haven't made that decision yet, actually we'll be discussing that in the coming weeks. But I would say that next year should be at the very max what we've spent this year. We haven't decided more precisely yet. We will guide you more precisely on the back of the Q4 numbers as far the brand spending is concerned.

Jonathan Crossfield - *Merrill Lynch - Analyst*

Okay that's great thanks Pierre-Jean.

Operator

The next question comes from Mr. Didier Scemama from ABN Amro, please go ahead with your question.

Didier Scemama - *ABN Amro - Analyst*

Yes good morning, it's Didier from ABN. Just one stupid question actually from me, as usual I guess. The 265 million asbestos can you suggest where you book that in the P&L on the US GAAP format?

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

Well it's booked, as far as the income statement is concerned, it's booked in other and as far as -- if you want to be more precise at the cost of -- at the income statement by nature, it is in cost of sales in the gross margin. So I think the answer is, when you look at our press release it is in the other line, right, and if you look at our cost of -- excuse me at our income statement in classified by nature of cost, it's included in costs of goods sold.

Didier Scemama - *ABN Amro - Analyst*

Okay, perfect thanks.

Operator

The next question comes from Mr. Simon Schafer from Goldman Sachs, please go ahead with your question.

Simon Schafer - *Goldman Sachs - Analyst*

Thanks for taking my question. Just looking at the pro forma analysis of NXP, I think it's apparent that there's a good amount of G&A costs that at some point on a pro forma basis go away from the parent company and will have to be digested by NXP. In reality obviously it'll take some time for those to come through, but I was wondering whether you can give us some detail as to how we should look at G&A as a percentage basis for the parent company now as we go into 2007?

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

Well it's hard for me to comment on the SG&A of NXP. I think with the higher cost in Q2 and Q3 obviously there were some costs, it was a very active G&A which was obviously spent on the back of the transaction everybody worked very hard on. Some of those costs were a part of the transaction costs but certainly there was a, I would say, some G&A activity there. Will it come down? Please bear with me, NXP is now a third party company in which own 19.9% so I will not guide you on NXP, bear with me, moving forward.

Simon Schafer - *Goldman Sachs - Analyst*

And then as a follow-up question, more on the balance sheet, obviously a very significant net cash position now and it's nice to see that you've found the ability to have, to schedule the EGM and get up to the 4 billion number that then will be redistributed through buybacks around the end of next year. But in light the pending disposals potentially of LG and TSM that will still leave you in a fairly underleveraged balance sheet situation. So I was wondering given that your previous statements have always been that your net debt equity would probably be capable of sustaining 25% or so, what does that mean in terms of potential scope for acquisitions or other means of redistribution of cash?

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

Yes, well let me, before I answer that, let me just say one word on the first part of your question which relates to the buybacks. So that, what we've done here and communicated to you is crystal clear. We announced 1.5 in July, you remember that, on the back of the Semi press release we announced that we would distribute 4 including the 1.5 but we left obviously, I would say pending, the way this would be split.

So in the meantime we've worked in order to get maximum tax efficiency actually on the whole amount, and the new piece of news -- there are two new pieces of news in this press release. The first piece of news is that we think that we will be able to buyback the full 4 billion in a tax efficient manner, I think that's the first piece of news. And the second piece of news is that given the accelerated pace of buyback we believe that by the end of 2006 we should be around 2.5 billion on our way to the 4 billion share buyback by the end of 2006.

I think those are the elements and of course as part of this process, as you've mentioned, we will have an EGM sometime in October to get our shareholders in line with this particular process. So that's the first answer, indeed those are the new pieces of news there.

Now as far as acquisitions are concerned, this leaves us with some cash in the balance sheet. I want you to realize that technically we have spent slightly shy of 900 million on the back of share buyback, on that particularly share buyback in the second half. We will be then spending another probably 1.6 billion to [grow] to the 2.5. The other thing we'll have to spend in the course of Q4 will be obviously the closing of Intermagnetics. So those are the expected cash disbursements in the fourth quarter of 2006.

Now moving forward we are looking at acquisitions, you know that. It's very hard to give an amount and it's very hard as well to give timing. This will be obviously only if it makes money and if it makes sense and it's hard to guide you much more on that. In terms of the split, if you look back at what we've done historically it's been 60% to shareholders and 40 plus reinvested in the business. I'm not saying it's a proxy moving forward but that's what we've done looking back.

And the last thing I want to say is, in terms of the segments we'll be looking at, nothing new there, we'll be looking at Lighting, we'll be looking at DAP Healthcare & [Wellness] and we'll be looking at Medical. And if and when it makes sense some very specific targets at Consumer Electronics and there as you've seen one of [inaudible] is Peripherals & Accessories. So that's as much as I can tell you as at today.

Now on the stakes, you've mentioned the stakes, the stakes will become available technically in the course of next year but there'll be issues of liquidity as well as target prices. We don't want to compromise on those stakes. And we will see how we can actually move on those stakes in order not to compromise on the value we expect from the portfolio for those two particular stakes.

Simon Schafer - *Goldman Sachs - Analyst*

Understood, thank you very much.

Operator

The next question comes from Mr. Antoine Badel from Credit Suisse, please go ahead with your question.

Antoine Badel - *Credit Suisse - Analyst*

Yes, good morning. I'd like to know what is on management's agenda for 2007? You've executed the Semiconductor divestiture, you're returning more cash to shareholders, operational performance is good as it is today. What can we look forward to as incremental opportunities for value creation next year?

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

Well I think I would say, and I'm not meaning to be funny there, I would say do it again. I think one of the reasons why we have a discount, you are the experts and for you to tell us. But what we understand is that the discounts attached to our stock is partly linked to the volatility of our numbers. So I think if we can prove now that we have refocused our portfolio on more predictable businesses we would hope that by delivering again in '07 the performance we are currently delivering in '06 that should help create some upside.

So I would say the first part of the answer is consistency and predictability out of a company which, I am sure you will agree with that, was perceived as not fully delivering on that particular angle.

The second element is to continue to grow in the high margin territories. If you look at Q3 and you spend one minute zooming PD by PD from Medical up 6% to Lighting up 10% with DAP in between growing 9%. With good margin in all of those three, our objective is to continue to grow in those particular product divisions with the kind of guidance we gave to you on margin in order to create value. Because the trick there will be in a predictable environment to continue to grow and then create obviously some value there.

The third element will be obviously to keep on taking care of shareholders as we've tried to do over the next, actually I would say, 12 months via obviously increase the attention there.

And the fourth element will be to basically manage our stakes in an efficient manner and make acquisition in a value creating manner. Those would be the elements which all will be on our agenda for next year.

Antoine Badel - *Credit Suisse - Analyst*

Thank you. And maybe a quick second question. I don't think you've broken out revenues in IFO for optical licensing [please]?

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

As you know we like to present the Consumer Electronics number as a package but that's why we don't put it in the press release but I will give it to you. The number for Q3 2006 was EUR38 million.

Antoine Badel - *Credit Suisse - Analyst*

Thank you.

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

Sorry, excuse me correction, EUR36 million.

Antoine Badel - *Credit Suisse - Analyst*

Thanks.

Operator

The next question comes from Mr. Thomas Brenier from Soci t G n rale, please go ahead with your question.

Thomas Brenier - *Societe Generale - Analyst*

Yes good morning. I've got a first question on the Medical division. I remember last quarter you told us that you were expecting order intake to grow north of sales growth. I understand it has grown about the same pace. So is that something that is disappointing for order intake? And do you expect this order intake to accelerate maybe in Q4?

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

Well I think my comment there was for the year. I think -- am I considering the 6% for Q3 disappointing? No. As we've said the -- as you know the first two, in particular the first quarter had been extremely high. These markets, and I go back to the first question on this Q&A which related to the comparison to GE, clearly this market grows at 4 to 5; 6% is a good number for incoming orders.

On the total year I would still hope that incoming orders would be north of the 6% guidance for revenue and I'm talking of incoming orders. Am I disappointed? No. So I can't add very much. I think what is interesting in Q3 is that if you zoom the good product divisions of Q3 were a little bit different in particular we did well in [MR] in that third quarter. So I think the interesting thing is, in that third quarter, beyond the fact that it was 6%, was the fact that it came -- the good numbers came from different businesses from the ones which were particularly strong in the first quarter. So I think it's not only the number but it's as well the mix of that particular number.

The other thing you should keep in mind, and we've disclosed that, because it's important for value creation on Stentor, is the very strong incoming orders for iSite. I think this is something to obviously watch. You know that the business models there will enable us to start delivering bottom line as we have guided you by Q4 next year. But it's particularly important to see that our backlog on the iSite ex-Stentor product is continuing to come in very strongly on the third quarter. That's important for Medical Informatics product group.

Thomas Brenier - *Societe Generale - Analyst*

Okay, thank you. My second question would be on Consumer Electronics. I just noted the number of employees is up significantly from Q2, I think 10% quarter-over-quarter. Is there something that explains this change?

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

Yes I think that's essentially seasonal. As you know Consumer Electronics, our model is very different. One of the reasons why we have a very low asset base and we have a low headcount which is open to fluctuation up, is because we've stripped off completed our business model essentially from [factories] and when we need to, we adjust upward on an as needed basis.

So basically it's done by attempts and in a way which can almost be treated, I would say, online, the following quarter. So don't read more than the fact that we had actually a strong activity versus what we had expected in Q3, which by the way translates in the margin of consumer electronics, and should not be seen as an increasing fixed cost, I would say, looking forward.

Thomas Brenier - *Societe Generale - Analyst*

Thanks a lot.

Operator

The next question comes from Mr. François Meunier from Cazenove, please go ahead with your question.

Francois Meunier - *Cazenove - Analyst*

Hello, good morning everyone. Just to come back to Consumer Electronics. I just wanted to have the exact number for licensing in Q3 and maybe you could recall what it was in Q2?

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

Okay. I think in Q3 I just actually mentioned it. I think it is EUR36 million. And for the second quarter of last year, give me one second, 45 million was the number for the second quarter of last year -- excuse me, for the second quarter this year.

Francois Meunier - *Cazenove - Analyst*

Okay thanks. And in terms of Medical, the year-on-year growth we are seeing is a bit slowing down from the peak we saw in Q4 and Q1 this year. It was closer to 14, 15%. Shall we read anything into that?

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

No I think we've had -- you're talking revenue or incoming orders? I'm assuming you're talking incoming orders.

Francois Meunier - *Cazenove - Analyst*

And revenues as well yes.

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

Revenue as well. Okay, incoming orders. What has happened, we had an extremely strong first quarter. We had obviously a lower second quarter and there we are with the third quarter at 6%. The guidance for the revenue growth of Medical is 6% and we confirm that. And as I mentioned, we should finish the year for '06 probably north of that 6%. So I think that there is absolutely nothing new there.

The market again of Medical grows at 4 to 5%. Some people were telling me again that [G] is guiding down. Okay, we are absolutely sticking to the guidance we gave to you which is 6% revenue growth for the year. And as I said, if anything in '06 we should be north of that.

Francois Meunier - *Cazenove - Analyst*

Okay so basically you should see a stabilization or a slight acceleration in Q4, that's what you're saying.

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

Well you will calculate backward what it gives for Q4 revenue. Now I'm talking revenue. The year should be indeed in a way that it enables us to finish north of 6%. So that enables you to calculate the kind of growth we should have in the fourth quarter.

Francois Meunier - *Cazenove - Analyst*

Thank you very much.

Operator

The next 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. Maybe my question has been answered but maybe on your tax rate, your P&L tax credit, could you maybe elaborate a bit on that? And give us some guidance for your expected tax rate for Q4 now your portfolio also has changed of course excluding Semiconductors?

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

Okay. I think the tax rate is severely impacted by lots of moves. The tax rate applied to the Medical, sorry to the asbestos one-off was I think 36.5%, if I remember correctly. Basically, for the year, I would continue to guide you, excluding this exceptional at a tax rate which should be in the region of 31 to 32%.

And for next year, we haven't looked at it yet and I will guide you for next year with the fourth quarter results. But as at today I can't see why there should be a very significant change there post-sale of Semiconductor. But we will have to re-do our numbers there in the coming weeks.

Unidentified Audience Member

Okay, thank you very much.

Operator

the next question comes from Mr. William Mackie from MainFirst, please go ahead with your question.

William Mackie - *MainFirst Bank AG - Analyst*

Yes, just two short questions, please. Firstly, could you give us a little more guidance on the non-recurring costs related to Sarbanes-Oxley that you incur this year?

And also, sticking with the development and regional overhead costs, once you exclude NXP can you provide a little more guidance on how the regional costs may develop as we move into '07, '08 on a normalized structure? Thank you.

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

Okay, the Sarbane-Oxley cost I would say, in, it's between -- the impact once we will be looking at the complete year, but the big bulk of those costs indeed came in Q3 as you, I'm sure you saw in our press release; I would say probably non-recurring, between 20 and 30 million. That would be my number for the non-recurring portion of Sarbane-Oxley cost which are accounted for on that line; Other.

That's the first question, now, to your second question. Guiding you on Other for next year. I want to say that, excluding, I think was it on Other, no, I think you are relating to headquarters so you are talking about unallocated, I think that was your question?

William Mackie - *MainFirst Bank AG - Analyst*

Exactly, yes. Yes.

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

On unallocated we have three territories, I think brand, I answered it earlier on in this call; we will guide you on brand, it will be at the max what we spend this year. How much more precisely I will guide you in a quarter from now.

On pension, I think it would be same probably max; what we spend this year probably, I would say, you know, around those numbers. And there as well we will guide you on the back of Q4 for the pension cost, but it should be in that territory.

For headquarter expenses, which is the bulk of the rest, there you have to isolate the one of course related to SOx. And the rest of the headquarter expenses, if you remember, we guided you on an objective of 1% of revenue, meaning that we would reduce those costs to take into consideration the fact that our portfolio doesn't include Semiconductor any more. And that we were going anyway, regardless of the change of portfolio, to continue to reduce those costs in central. So that's the guidance I can give you on unallocated.

William Mackie - *MainFirst Bank AG - Analyst*

Thank you.

Operator

The last question comes from Mr. [Bert van Dijk from Het Financieel Dagblad]. Please go ahead with your question.

Bert van Dijk - *Het Financieel Dagblad - Journalist*

Good morning, sir. I just wanted to clarify on the asbestos claims or charge, I was just wondering, is it correctly to assume that there will be no additional charges in the coming quarters for those asbestos claims?

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

Well that is the plan. In reality on asbestos there is nothing new beside the fact, I mean, it has been disclosed, as you know, ever since '02. Let's go back to '81, that's not a new problem in Philips, it's been -- there are full disclosure in our annual report for the last three years. I think what is new is really two things; one is the fact that the legislation which many people expected until quite recently was actually waived, that's the way we understand it.

And the other thing is that with the help of external experts we were capable of simulating what we expect the cost to be for us net of reimbursement over the next ten years. So the one-off charge of 265 million we took, net charge, we took in Q3 is expected to cover us from that particular perspective for the next ten years.

Bert van Dijk - *Het Financieel Dagblad - Journalist*

Okay. And then the last follow-up question, I was just wondering if you could give me the figure of the new product sales as a percentage of total sales?

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

Well, you are taking me off guard there. The objective is -- was disclosed; if you go back to our slide of January, which is, I think still on our website, you will see the objective we have given ourselves for the year, which I will give you in one minute. From what I know, I believe we will reach that objective, I think we'll have to give you that online -- offline, Alan will give that to you.

Bert van Dijk - *Het Financieel Dagblad - Journalist*

Okay.

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

We will definitely make the objective; I think on Q2 we were at 55% and our objective is to increase, versus last year, by a couple of percentage points and we will reach that objective. So, if you look at the objective we disclosed to you in January, like-for-like, we will make the objective of a new -- of a ratio of new product sales, which is defined as products which have been introduced for less than two years, we will reach or exceed that objective we gave you at the time.

Bert van Dijk - *Het Financieel Dagblad - Journalist*

Okay. Thanks.

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

I think, if you don't mind, I think we have to go now, unless there is any more questions?

Operator

Mr. Sivignon, there are no further questions.

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

Okay, that's what I had understood. So I thank you very much and if there is any further questions, as usual of course, Alan Cathcart will be more than happy to obviously answer the additional questions. Thank you very much. Goodbye.

Operator

This concludes the Royal Philips Electronics Third Quarter Results call on Monday October 16, 2006. Thank you for participating, you may now disconnect.
