KONINKLIJKE PHILIPS ELECTRONICS NV
Form 20-F
February 24, 2012
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As filed with the Securities and Exchange Commission on February 24, 2012

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

Form 20-F

(Mark one)

¨ **REGISTRATION STATEMENT PURSUANT TO SECTION 12(b) OR (g) OF THE SECURITIES EXCHANGE ACT OF 1934**

OR

x **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the fiscal year ended December 31, 2011

OR

¨ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

OR

¨ **SHELL COMPANY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
Commission file number 001-05146-01

KONINKLIJKE PHILIPS ELECTRONICS N.V.

(Exact name of Registrant as specified in charter)

ROYAL PHILIPS ELECTRONICS

(Translation of Registrant s name into English)

The Netherlands

(Jurisdiction of incorporation or organization)

Breitner Center, Amstelplein 2, 1096 BC Amsterdam, The Netherlands

(Address of principal executive office)

Eric Coutinho, Chief Legal Officer & Secretary to the Board of Management

+31 20 59 77232, eric.coutinho@philips.com, Breitner Center, Amstelplein 2, 1096 BC Amsterdam, The Netherlands

(Name, Telephone, E-mail and/or Facsimile number and Address of Company Contact Person)

Securities registered or to be registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Common Shares par value Euro (EUR) 0.20 per share	New York Stock Exchange

Securities registered or to be registered pursuant to Section 12(g) of the Act:

None

Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act:

None

(Title of class)

Indicate the number of outstanding shares of each of the issuer s classes of capital or common stock as of the close of the period covered by the annual report:

Class	Outstanding at December 31, 2011
Koninklijke Philips Electronics N.V.	1,008,975,445 shares, including
Common Shares par value EUR 0.20 per share	82,880,543 treasury shares

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. x Yes ¨ No

If this report is an annual or transition report, indicate by check mark if the registrant is not required to file reports pursuant to section 13 or 15(d) of the Securities Exchange Act of 1934. ¨ Yes x No

Note-Checking the box above will not relieve any registrant required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 from their obligations under those Sections.

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. x Yes ¨ No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). ¨ Yes ¨ No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer x Accelerated filer ¨ Non-accelerated filer ¨

Indicate by check mark which basis of accounting the registrant has used to prepare the financial statements included in this filing:

U.S. GAAP ¨ International Financial Reporting Standards as issued by by the International Accounting Standards Board x Other ¨

If Other has been checked in response to the previous question, indicate by check mark which financial statement item the registrant has elected to follow. ¨ Item 17 ¨ Item 18

If this is an annual report, indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). ¨ Yes x No

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IFRS basis of presentation

The financial information included in this document is based on IFRS, unless otherwise indicated.

Forward-looking statements and other information

Please refer to the Forward-looking statements and other information, in the introduction of this report for more information about forward-looking statements, third-party market share data, fair value information, IFRS basis of preparation, use of non-GAAP information, statutory financial statements and management report, and reclassifications.

Dutch Financial Markets Supervision Act

This document comprises regulated information within the meaning of the Dutch Financial Markets Supervision Act *(Wet op het Financieel Toezicht).*

Statutory financial statements and management report

The chapters Group financial statements and Company financial statements contain the statutory financial statements of the Company. The introduction to the chapter Group financial statements sets out which parts of this Annual Report form the Management report within the meaning of Section 2:391 of the Dutch Civil Code (and related Decrees).

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Introduction

This document contains information required for the annual report on Form 20-F for the year ended December 31, 2011 of Koninklijke Philips Electronics N.V. (the 2011 Form 20-F.) Reference is made to the Form 20-F cross reference table herein. Only (i) the information in this document that is referenced in the Form 20-F cross reference table, (ii) the cautionary statement concerning forward-looking statements and explanation on use of non-GAAP information on the next two pages and (iii) the Exhibits shall be deemed to be filed with the Securities and Exchange Commission for any purpose. Any additional information herein which is not referenced in the Form 20-F cross reference table, or the Exhibits themselves, shall not be deemed to be so incorporated by reference, shall not be part of the 2011 Form 20-F and is furnished to the Securities and Exchange Commission for information only.

The terms Philips , the Group , we , our and us refer to the Company and as applicable to its subsidiaries and or its interest in joint ventures an associates.

IFRS based information

The audited consolidated financial statements as of December 31, 2011 and 2010, and for each of the years in the three-year period ended December 31, 2011, included in the 2011 Form 20-F have been prepared in accordance with International Financial Reporting Standards (IFRS) as endorsed by the European Union (EU). All standards and interpretations issued by the International Accounting Standards Board (IASB) and the IFRS Interpretations Committee effective year-end 2011 have been endorsed by the EU, except that the EU did not adopt certain paragraphs of IAS 39 applicable to certain hedge transactions. Philips has no hedge transactions to which these paragraphs are applicable. Consequently, the accounting policies applied by Philips also comply fully with IFRS as issued by the IASB.

Non-GAAP information

In presenting and discussing the Philips Group s financial position, operating results and cash flows, management uses certain non-GAAP financial measures such as: comparable growth; adjusted income from operations; net operating capital; net debt; cash flow before financing activities; net capital expenditures and free cash flow. These non-GAAP financial measures should not be viewed in isolation as alternatives to the equivalent IFRS measure and should be used in conjunction with the most directly comparable IFRS measure(s). Reference is made to the section titled Use of non-GAAP information for further information.

Third-party market share data

Statements regarding market share, contained in this document, including those regarding Philips competitive position, are based on outside sources such as specialized research institutes, industry and dealer panels in combination with management estimates. Where full year information regarding 2011 is not yet available to Philips, those statements may also be based on estimates and projections prepared by outside sources or management. Rankings are based on sales unless otherwise stated.

Fair value information

In presenting the Philips Group s financial position, fair values are used for the measurement of various items in accordance with the applicable accounting standards. These fair values are based on market prices, where available, and are obtained from sources that are deemed to be reliable. Readers are cautioned that these values are subject to changes over time and are only valid at the balance sheet date. When quoted prices or observable market values do not exist, fair values are estimated using valuation models, which we believe are appropriate for their purpose. They require management to make significant assumptions with respect to future developments which are inherently uncertain and may therefore deviate from actual developments. Critical assumptions used are disclosed in the financial statements. In certain cases, independent valuations are obtained to support management s determination of fair values.

Documents on display

It is possible to read and copy documents referred to in the 2011 Form 20-F that have been filed with the SEC at the SEC s public reference room located at 100 F Street, N.E., Room 1580, Washington, D.C. 20549. Please call the SEC at 1-800-SEC-0330 for further information on the public reference rooms and their copy charges. Philips SEC filings are also publicly available through the SEC s website at www.sec.gov.

For definitions and abbreviations reference is made to chapter 18, Definitions and abbreviations, of this report.

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Introduction

Forward-looking statements

Pursuant to provisions of the United States Private Securities Litigation Reform Act of 1995, Philips is providing the following cautionary statement.

This document, including the information referred to in the Form 20-F cross reference table, contains certain forward looking statements with respect to the financial condition, results of operations and business of Philips and certain of the plans and objectives of Philips with respect to these items, in particular, among other statements, certain statements in Item 4 Information on the Company with regard to management objectives, market trends, market standing, product volumes, business risks, the implementation of our Accelerate! program, the statements in Item 8 Financial Information relating to legal proceedings, the statements in Item 5 Operating and financial review and prospects with regard to trends in results of operations, margins, overall market trends, risk management, exchange rates and statements in Item 11 Quantitative and qualitative disclosures about market risks relating to risk caused by derivative positions, interest rate fluctuations and other financial exposure are forward-looking in nature. Forward-looking statements can be identified generally as those containing words such as anticipates , assumes , believes , estimates , expects , should , will , will likely result , forecast , outlook , projects , may or similar expressions. By their na forward-looking statements involve risk and uncertainty, because they relate to events that depend on circumstances that will occur in the future. There are a number of factors that could cause actual results and developments to differ materially from those expressed or implied by these forward-looking statements.

These factors include, but are not limited to, domestic and global economic and business conditions, developments within the euro zone, the successful implementation of our strategy and our ability to realize the benefits of this strategy, our ability to develop and market new products, changes in legislation, legal claims, changes in exchange and interest rates, changes in tax rates, pension costs and actuarial assumptions, raw materials and employee costs, our ability to identify and complete successful acquisitions and to integrate those acquisitions into our business, our ability to successfully exit certain businesses or restructure our operations, the rate of technological changes, political, economic and other developments in countries where Philips operates, industry consolidation and competition.

As a result, Philips actual future results may differ materially from the plans, goals and expectations set forth in such forward-looking statements. For a discussion of factors that could cause future results to differ from such forward-looking statements, reference is made to the information in Item 3D Risk Factors .

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Use of non-GAAP information

Koninklijke Philips Electronics N.V. (the Company) believes that an understanding of sales performance is enhanced when the effects of currency movements and acquisitions and divestments (changes in consolidation) are excluded. Accordingly, in addition to presenting nominal growth , comparable growth is provided.

Comparable sales exclude the effects of currency movements and changes in consolidation. As indicated in the section 12.10, Significant accounting policies, sales and income are translated from foreign currencies into the Company s reporting currency, the euro, at the exchange rate on transaction dates during the respective years. As a result of significant currency movements during the years presented, the effects of translating foreign currency sales amounts into euros could have a material impact on our sales figures. Therefore, these impacts have been excluded in arriving at the comparable sales in euros. Currency effects have been calculated by translating previous years foreign currency sales amounts into euros at the following year s exchange rates in comparison with the sales in euros as historically reported. The years under review were characterized by a number of acquisitions and divestments, as a result of which activities were consolidated or deconsolidated. The effect of consolidation changes has also been excluded in arriving at the comparable sales. For the purpose of calculating comparable sales growth, when a previously consolidated entity is sold or contributed to a venture that is not consolidated by the Company, relevant sales are excluded from impacted prior-year periods. Similarly, when an entity is acquired, relevant sales are excluded from impacted periods.

Philips discusses adjusted income from operations in the 2011 Form 20-F. Adjusted income from operations represents income from operations before amortization and impairment of intangible assets generated in acquisitions (excluding software and capitalized development expenses).

The Company uses the term adjusted income from operations to evaluate the performance of the Philips Group and its sectors. Referencing adjusted income from operations is considered appropriate in light of the following:

Philips has announced that one of its strategic drivers is to increase profitability through re-allocation of its resources towards opportunities offering more consistent and higher returns. Moreover, Philips intends to redeploy capital through value-creating acquisitions. Since 2006, management has used the adjusted income from operations measurement internally to monitor performance of the businesses on a comparable basis. As of 2007, Philips has also set external performance targets based on this measurement as it will not be distorted by the unpredictable effects of future, unidentified acquisitions.

Non US investors are advised that such presentation is different from the terms used in Philips results announcements and 2011 Annual Report.

Philips believes that an understanding of the Group s financial condition is enhanced by the disclosure of net operating capital (NOC), as this figure is used by Philips management to evaluate the capital efficiency of the Philips Group and its operating sectors. NOC is defined as: total assets excluding assets from discontinued operations *less:* (a) cash and cash equivalents, (b) deferred tax assets, (c) other (non)-current financial assets, (d) investments in associates, and *after deduction of:* (e) provisions excluding deferred tax liabilities, (f) accounts and notes payable, (g) accrued liabilities, (h) current/noncurrent liabilities, and (i) trading securities.

Net debt is defined as the sum of long- and short-term debt minus cash and cash equivalents. The net debt position as a percentage of the sum of group equity (shareholders equity and non-controlling interests) and net debt is presented to express the financial strength of the Company. This measure is widely used by management and investment analysts and is therefore included in the disclosure.

Cash flows before financing activities, being the sum total of net cash from operating activities and net cash from investing activities, and free cash flow, being net cash from operating activities minus net capital expenditures, are presented separately to facilitate the reader s understanding of the Company s funding requirements.

Net capital expenditures comprise of purchase of intangible assets, expenditures on development assets, capital expenditures on property, plant and equipment and proceeds from disposals of property, plant and equipment. This measure is widely used by management to calculate free cash flow.

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Form 20-F cross reference table

Only (i) the information in this document that is referenced in the Form 20-F cross reference table, (ii) the introductory information (including the cautionary statements concerning Forward-looking statements and explanation on use of non-GAAP information) on pages 5-7 of this report, and (iii) the Exhibits shall be deemed to be filed with the Securities and Exchange Commission for any purpose. The content of Philips websites and other websites referenced herein should not be considered to be a part of or incorporated into the 2011 Form 20-F. Any additional information which is not referenced in the Form 20-F cross reference table or the Exhibits themselves shall not be deemed to be so incorporated by reference, shall not be part of the 2011 Form 20-F and is furnished to the Securities and Exchange Commission for information only.

The table below sets out the location in this document of the information required by SEC Form 20-F. The exact location is included in the column Location in this document . The column Page includes the starting page of the section/paragraph for reference only.

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Performance highlights

Prior years results and cash flows have been restated to reflect the effect of classifying the Television business as discontinued operations in 2011.

Financial table

all amounts in millions of euros unless otherwise stated

	2009	**2010**	**2011**
Sales	20,092	22,287	22,579
Adjusted IFO[1)]	1,096	2,562	1,680
as a % of sales	5.5	11.5	7.4
IFO	660	2,080	(269)
as a % of sales	3.3	9.3	(1.2)
Net income (loss)	424	1,452	(1,291)
per common share in euros			
- basic	0.46	1.54	(1.36)
- diluted	0.46	1.53	(1.36)
Net operating capital[1)]	12,649	11,951	10,427
Free cash flows[1)]	763	1,356	(108)
Shareholders equity	14,595	15,046	12,355
Employees at December 31[2)]	116,153	119,775	125,241
of which discontinued operations	4,764	3,610	3,353

1) For a reconciliation to the most directly comparable GAAP measures, see chapter 15, Reconciliation of non-GAAP information, of this report
2) Adjusted to reflect a change of employees reported in the Healthcare sector for the past periods
3) For a definition of mature and growth geographies, see chapter 18, Definitions and abbreviations, of this report

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Performance highlights

Operating cash flows

in millions of euros

Net debt (cash) to group equity[1)]

in billions of euros

Employee Engagement Index

% favorable

Sales of Green Products

as a % of total sales

Operational carbon footprint

in kilotons CO_2-equivalent

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Message from the CEO

Accelerate! is all about bringing meaningful innovations to our customers in local markets and doing so faster and better than the competition!
Frans van Houten, CEO

Dear stakeholder,

Philips is a great company with a wealth of talent and powerful assets e.g. outstanding innovation capabilities, a strong brand, a global footprint, leading positions in healthcare, lighting and lifestyle growth businesses, and a solid balance sheet. We have tremendous potential in terms of margin improvement, growth and higher returns. But as our 2011 results reaffirmed, we cannot be satisfied with our current performance, and we will step up to deliver fully on that potential.

In September 2011 we celebrated 120 years of Philips innovation a landmark achievement. 2011 was also a year of radical change, both on the world stage and within our company. It was the first year of Accelerate! a fundamental change and performance improvement program designed to unlock our full potential, and so make Philips an even stronger company capable of bringing meaningful innovations to market for many years to come. Together with my colleagues on the Executive Committee our new leadership team, spanning businesses, markets and functions I am honored to lead our company through this transformation and am encouraged by the start we have made to what will be a multi-year journey to a bright future.

Despite a challenging and volatile economic environment and ongoing market weakness, especially in Europe, important parts of the company performed well in 2011, and we ended the year with strong balance sheet and cash positions. At the same time, across the company near- term operational issues are being tackled with vigor and urgency. Our passion to improve and aim higher is shared by our 120,000 employees.

At Group level, we achieved 4% comparable sales growth at the lower end of our mid-term performance bandwidth, but with a strong contribution from growth geographies (33% of sales, up from 31% in 2010) and Green Products (39% of sales).

At 7.4% of sales, reported Adjusted IFO was below our mid-term 2013 profitability target, primarily due to continued pressure on gross margins, as well as higher costs and non-recurring charges related to, for example, inventory adjustments. Earnings were also impacted by investments for growth to drive market penetration and accelerate innovation. These include an investment of some EUR 470 million in Green Innovation.

Each year we review and assess the value of past acquisitions. Last year s analysis found the economy posed a higher risk, with recovery slow and uncertain. We adjusted our business plans and discount rates accordingly, resulting in an impairment of EUR 1.4 billion in the second quarter.

One of the major developments in 2011 was the signing of an agreement to transfer our Television business to a joint venture with TPV, in which we will hold a 30% stake. This joint venture will leverage the strengths of both companies to improve the position of Philips Television in the market, and will enable us to focus on expanding leadership positions in health and well-being markets across our three operating sectors. The deal is expected to close at the end of the first quarter of 2012 after the necessary merger clearance and governmental approvals are obtained.

In 2011 we concluded a number of acquisitions, primarily aimed at strengthening our product portfolio in growth geographies. I would like to welcome all our new employees from these acquisitions to Philips.

Reflecting our confidence in our plans to step up profitability and free cash flow through organic growth and operational excellence, we launched a EUR 2 billion share buy-back program in the summer. This will also improve the efficiency of our balance sheet. By the end of the year we had completed 35% of this program, which will run until the end of the second quarter of 2013.

As a further sign of our confidence in Philips future, we are proposing to the upcoming General Meeting of Shareholders to maintain this year s dividend at EUR 0.75 per common share, in cash or stock resulting in a yield (as of December 31, 2011) of 4.6% for shareholders.

Accelerate! the journey to unlock our full potential

For the past 120 years our meaningful innovations have improved the quality of life for millions, creating a strong and trusted Philips brand with market access all over the world. But with lack of consistent growth in recent years, and lean, agile new competitors winning over customers, it was clear that we urgently needed to speed up in order to improve our performance and competitiveness.

To this end, in the second quarter of 2011 we launched our Accelerate! program the first step on our journey to unlock our full potential and seed the ground for our future success. Accelerate! aims to significantly boost profitable growth by stepping up meaningful innovation and competitiveness, expanding margins, driving productivity and reducing complexity and working capital. It is designed to ensure that we empower and strengthen our customer-facing teams to win profitable market share, that we reduce complexity costs and deliver our innovations faster and more efficiently along the end-to- end chain to the customer, that we drive performance with transparency and accountability for granular business/market plans. And that we carry through our

strategies with the resources and determination to win our critical market battles and achieve leadership in our chosen markets.

Of course, making the turn to growth also requires a new, shared mindset a customer-focused, agile, can-do mentality. And with Accelerate! we are creating a new performance and growth culture centered around three key behaviors *Eager to win, Take ownership* and *Team up to excel* that are crucial for success and anchored by our General Business Principles.

With Accelerate! providing the roadmap toward growth, in the summer of 2011 we announced our mid-term performance goals, to be realized by the end of 2013:

- Comparable sales growth CAGR of 4-6%, assuming real GDP growth of 3-4% per annum
- Reported Adjusted IFO margins of 10-12% for the Group; 15-17% for Healthcare; 8-10% for Consumer Lifestyle (excluding unrelated licenses); 8-10% for Lighting
- Return on invested capital of 12-14%

Progress on our path to value by 2013

A key part of Accelerate! has been the implementation of our new operating model, the Philips Business System, which defines how all parts of the company should work together to create a faster, less complex and more competitive Philips. This system has begun to improve granular performance insights, enhancing transparency and management accountability, and enabling rapid corrective action where required.

We also needed to free up money to invest in our customer-facing activities and innovation and so pave the way for profitable growth. For this purpose, we are optimizing all overhead and support costs not directly involved in the operational customer value chain. This will create a lighter overhead structure comprising a single value-adding layer above the businesses, thereby reducing complexity and speeding up decision-making. It will also enable a cost saving of EUR 800 million by 2014. The overhead cost reduction program is on track, with the first savings already visible in the fourth quarter of 2011. In order to resource to win we are also making a targeted additional investment of EUR 200 million to increase the number of business/market combinations in which we are the outright leader.

Customer-centricity is an integral element of Accelerate! Across Philips, we are empowering and strengthening our customer-facing teams to win in markets by delivering superior products and services that meet the specific needs of local populations and bringing them to market faster. To this end, for example, we moved the leadership of our Kitchen Appliances business to Shanghai and acquired leading kitchen appliances companies Preethi (India) and Povos (China) in 2011. This will ensure we are better placed to harvest local consumer insights and match our competitors time-to-market.

One of the key drivers of our Accelerate! journey is the strengthening of our end-to-end customer value chain . We can only speed up our time-to-market and become truly competitive if we take a holistic view from product idea and manufacturing to order intake and delivery. Philips is transforming itself from a predominantly functional organization to a process-driven end-to-end collaboration model, embracing business excellence principles such as LEAN. This should allow us to deliver innovations to market much faster and at lower cost and with lower working capital. Pilots at Lighting, for instance, show that the collaborative end-to-end approach is having a significant impact. Breakthroughs in factory and demand planning, for example, mean our business group Lamps no longer needs to stock the majority of its portfolio in commercial warehouses, but instead packs to order , which allows much lower inventory levels and, ultimately, better profitability. And this approach offers our customers increased service flexibility, thanks to improved response times.

We are pleased that people engagement continues to be high and that Philips is able to attract and retain outstanding talent to strengthen the company. Our new behaviors central to our efforts to establish a culture of entrepreneurship and accountability have been made an integral part of our employee performance appraisal and reward system. And the incentive system for our executives has been changed to reflect line-of-sight accountability and is now fully aligned with the key performance indicators of our 2013 mid-term financial targets.

We also continued to deliver on our EcoVision sustainability commitments in 2011, as we strive to bring care to more than 500 million people, to improve the energy efficiency of our overall portfolio by 50%, and to double the global collection and recycling of our products, as well as the amount of recycled materials in our products. Our sustainability performance received widespread recognition during the year. For instance, *Newsweek* named Philips the 9th greenest company in the world, we regained our sector and super-sector leadership in the Dow Jones Sustainability Index, and our

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Lighting sector received a United Nations Leader of Change Award for its contribution to sustainable lighting solutions.

Looking forward

Our mission remains to improve people s lives through meaningful innovation. And we have now tightened the vision that guides us:

At Philips, we strive to make the world healthier and more sustainable through innovation. Our goal is to improve the lives of 3 billion people a year by 2025. We will be the best place to work for people who share our passion. Together we will deliver superior value for our customers and shareholders.

In light of key global trends and challenges e.g. the demand for affordable healthcare, the energy efficiency imperative, and people s desire for personal well-being we are confident in our chosen strategic direction.

We have a focused portfolio, with strong potential in both mature and growth geographies such as China and India. The large majority of our businesses have the right fundamentals for profitable growth, and we are seeing growth in our core businesses. And where there are pressing operational issues, we are working tirelessly to turn things round and increase productivity.

The value potential in our portfolio is underpinned by talent and strong assets. As demonstrated at our Innovation Experience event, held in September 2011 to mark 120 years of Philips, our innovation and design capabilities are rightly world-renowned, and we hold strong technology and intellectual property positions. In 2011 we also secured our highest-ever placing (41st) on the annual Interbrand ranking of the world s most valuable brands, as well as being named one of China s top ten consumer brands by Superbrands. And, crucially, we have capable and motivated people and leadership: our 2011 Employee Engagement Survey showed an Employee Engagement Index of 76%, down one percentage point, and a People Leadership Index of 78%, up two percentage points. And all of this is supported by a solid balance sheet.

We are still in the early stages of a multi-year transformation of our company, and I am delighted that the organization is responding well to the Accelerate! initiatives. Accelerate! will drive granular execution of our plans and enable the necessary investments in innovation, people, systems, and markets to deliver profitable growth and return on invested capital. And we will reap the benefits of our new culture of entrepreneurship and accountability, and commitment to business excellence.

We are cautious about 2012, given the uncertainty in the global economy, and Europe in particular. In addition, we expect our 2012 results to be affected by the previously communicated restructuring charges and one-time investments aimed at improving our business performance trajectory, as part of Accelerate! Excluding these additional charges, we anticipate that underlying operating margins and capital efficiency in the sectors will improve in the latter part of 2012. While we are concerned about the economic environment, all of us at Philips are fully committed to improve our operational performance to achieve our mid-term (2013) financial targets.

On behalf of the Executive Committee, I would like to thank our customers for their loyalty to Philips over this past year. I would also like to thank all our employees for their hard work as well as for their willingness to embrace change. And finally I would like to thank our other stakeholders, in particular our shareholders, for their continued support in these challenging times. We have set out on a demanding and exciting journey. More than ever, we are resolved to accelerate, unlock Philips full potential, and grow the value of your investment.

Frans van Houten,

Chief Executive Officer

1 Our company

Philips is a diversified company active in the markets of healthcare, consumer lifestyle and lighting, and headquartered in Amsterdam (Netherlands).

Our heritage

Philips was founded in Eindhoven (Netherlands) in 1891 by brothers Anton and Gerard Philips to manufacture incandescent lamps and other electrical products . For the 120 years since then, we have been enhancing people s lives with a steady flow of ground-breaking innovations. And we are determined to build upon this rich heritage as we aspire to touch billions of lives each year with our innovative lighting and healthcare solutions and our consumer lifestyle products.

Our mission

Improving people s lives through meaningful innovation

Innovation is integral to everything we do. But innovation does not only mean new technology . It can also mean a new application, a new business model or a unique customer proposition brought about by an innovative partnership. By tracking global trends and understanding the challenges facing people in their daily lives, we ensure that people s needs and aspirations are at the heart of our innovation endeavors.

Our vision

At Philips, we strive to make the world healthier and more sustainable through innovation. Our goal is to improve the lives of 3 billion people a year by 2025. We will be the best place to work for people who share our passion. Together we will deliver superior value for our customers and shareholders.

Our domain

We operate in the health and well-being domain.

We seek to improve the quality of people s lives through focusing on their health and well-being.

By health we mean not only medical aspects of health, but also keeping fit, having a healthy diet, and generally living a healthy lifestyle. By well-being we mean a general sense of fulfillment, feeling good and at ease. Well-being also refers to the sense of comfort, safety and security people feel in their environment at home, at work, when shopping or on the road. Our focus on health and well- being also implies helping to build a sustainable society.

Our behaviors

In 2011 we adopted a new set of behaviors:

- Eager to win
- Take ownership

Team up to excel

Our new behaviors are designed to foster a new performance culture and help all of us accelerate to deliver sustainable profitable growth always in compliance with Philips General Business Principles.

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2 Our strategic focus

In a fast-changing world, we are committed to returning superior value to our stakeholders. We will achieve this through leadership in innovation, an absolute focus on the customer, local market relevance, and operational excellence, while costs need to be at least in line with our competitors.

We aim to create value through a deep understanding of our businesses and markets and by building sustainable competitive advantage in each business. In doing so, we will leverage the strengths of the Philips Group e.g. talented people, outstanding innovation capabilities, a strong brand, a global footprint, leading market positions and a solid balance sheet to deliver global leadership and benchmark performance.

Accelerate!

In 2011 we launched Accelerate! our comprehensive change and performance improvement program. The aim of Accelerate! is to create an agile and entrepreneurial Philips. A company with satisfied customers and employees with fulfilling roles. A company that grows and delivers consistent shareholder value. During the year we managed to put many of our Accelerate! enablers in place:

- We are becoming increasingly customer-centric, focused on meeting local market needs.

- We apply granular performance planning and management to realize operating plans that are resourced to win.

- We are transforming Philips from a predominantly functionally orientated organization to one whereby we seamlessly operate along integrated, lean end-to-end customer value chain processes between global businesses and local market teams, so that we deliver with speed and excellence.

- We are reshaping our operating model for simplicity and speed. The Philips Business System provides us with a blueprint for the company s way of working.

- We are establishing a growth and performance culture in which people are eager to win, take ownership, and team up to excel; our incentive and reward systems recognize sustained performance and the right behavior.

Seizing market opportunities

With a deep understanding of many of the longer-term challenges our world faces from aging populations to the need for efficient energy usage and the desire for personal well-being and the innovative capability to address these challenges, we strongly believe we can continue to make a meaningful contribution to people s lives.

Our strong position in many promising markets, coupled with our innovation pipeline, powerful brand and engaged workforce, puts us in an excellent position for the future.

Our sectors

We strive for a balanced portfolio of businesses that have or can attain global leadership positions and deliver performance at benchmark levels.

Healthcare: The future of healthcare is one of the most pressing issues of our time. Philips Healthcare is committed to providing meaningful innovations that improve the quality of care, enhance patients lives and enable the delivery of better outcomes at lower cost. Our growth strategy is grounded in a fundamental belief that clinical excellence and continuous innovation around the patient experience can fundamentally change healthcare as we know it. Our competitive advantage lies in our clinical perspective, the broad clinical subject-matter expertise within the company, as well as the deep clinical relationships we have with our customer base. This allows us to deliver solutions expertly tuned to the needs of the clinician as well as the financial and operational needs of healthcare administrators, payers, regulators and purchasing organizations by enabling a connected and holistic view of care delivery that tangibly and transparently improves clinical outcomes.

Consumer Lifestyle: Across the world, consumers want to maintain and improve their health and well- being and that of their families. To achieve this, they look for propositions that will improve their lives from brands that they trust. Philips Consumer Lifestyle is on a journey to become a leading player in health and well-being. We have a global footprint, with an established presence in both mature and growth geographies. We have a leading global brand, which is highly trusted across the world. Consumer Lifestyle makes a difference to people s lives by making it easier for them to achieve a healthier and better lifestyle.

Lighting: Human life revolves around light. Light affects our mood, improves our well-being, and enables us to experience and achieve more. It is a vital part of making our lives fuller, more productive and safer. Our Lighting sector focuses on innovative ways of using light to enhance people s lives where they live and work at home, at school, at work, in shops and public places, as well as on the road. Recognizing how resource conservation and climate protection will play an increasingly significant part in human health and well- being, we pay special attention to maximizing the effect of lighting while minimizing the energy required to produce it.

Our market opportunity

Global trends and challenges

Ongoing focus on growth geographies

Growth geographies are vitally important to Philips. As the number of middle-class households in these markets grows, we expect demand for our products to increase as people have more money to spend on feeling and staying healthy. Therefore, we will continue to make sure we address local needs effectively and to invest in having the right capabilities and resources in place to win in these growth geographies.

We want to be seen as clear leaders in sustainability

We are committed to being a leading company in matters of sustainability. We look at sustainability through the lenses of our sectors and define specific ambitions (to be realized by the end of 2015) for each of them: bring care to 500 million people; improve the energy efficiency of our overall portfolio by 50%; double the global collection and recycling amounts of Philips products as well as the amount of recycled materials in our products.

Our mid-term 2013 financial targets

We measure value through a balanced combination of sales growth and return on invested capital (driven by Adjusted IFO, capital turns and free cash flow) in conjunction with other financial, operational and strategic key performance indicators.

Our mid-term financial targets (to be realized by the end of 2013):

- Comparable sales growth CAGR of 4-6%, assuming real GDP growth of 3-4% per annum
- Reported Adjusted IFO margins of 10-12% for the Group; 15-17% for Healthcare; 8-10% for Consumer Lifestyle (excluding unrelated licenses); 8-10% for Lighting
- Return on invested capital of 12-14%

3 Our strategy in action

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Philips China journey a dynamic partnership

China faces a major challenge as it works to provide healthcare to more than 1.3 billion people. We are committed to helping the Chinese medical community find answers to China s healthcare needs through innovative technology solutions.

As its population grows and its middle class expands, China faces a huge societal and fiscal challenge: how to provide high-quality cost-effective healthcare to over 1.3 billion people? China is working to meet three key strategic goals. First, it must grow its healthcare system to provide basic medical services for all, particularly in under-served regions. Second, its medical community must find solutions to address the different needs of the emerging middle class. Finally, it must achieve these goals while keeping its remarkable economic growth on track. China s decision to make major investments in the expansion of its healthcare infrastructure is an important step on this journey to provide accessible, affordable care for its people.

Meaningful solutions for changing healthcare demands

As a leading healthcare innovator, Philips has a unique ability and opportunity to help China improve the health and well-being of its people. Starting in 2007, our China Team worked with China s medical community and government to identify the country s primary needs and develop innovative technology solutions to meet their Changing healthcare demands. We began our journey by listening. What we heard was that our customers wanted more clinical benefits from imaging systems and more research collaboration between Philips and China s great university hospitals. Out of these conversations have come ongoing peer-to-peer engagements, continuing education workshops, customer appreciation events and perhaps most important, dynamic, ongoing research.

As we began this journey, we also set a goal for ourselves: to become one of the CT and MR market leaders in China. Today, our CT and MR offerings serve a wide range of needs in environments from rural community hospitals to the country s leading teaching hospitals. The cooperative effort within our China Team encompassing our MR and CT businesses, sales and service and targeted collaborations with customers got us to our goal of becoming one of the imaging technology leaders in China.

The Center for Biomedical Imaging Research at Tsinghua University chose Philips 3T Achieva TX as its main research scanner, says Chun Yuan, Ph.D, the Center s Director. With the help of many different branches within Philips, especially Philips China, and through scientific collaboration, our researchers were able to start active imaging research in several focus areas in cardiovascular, tumor and neurological imaging.

The success of our CT and MR business s China journey is reflected in its growth performance, with sales tripling in the period 2007-2010. This momentum continued in 2011, with a double-digit annual growth rate.

We are succeeding in China because our focus extends beyond sales. We are committed to enhancing patients lives through our clinical expertise and working with our customers to improve the ability to deliver care. With our complete imaging portfolio, today we are even better positioned to help China meet its growing clinical care needs. The next phase of the journey? China plans to make significant investments in county-level hospitals and in digitization to improve healthcare informatics and clinical decision support. As a global healthcare leader and working partner with China, Philips will be there every step of the way.

COPD home care solutions: Philips delivers

Chronic obstructive pulmonary disease, a life-threatening lung disorder, affects nearly 600 million people. Philips   comprehensive portfolio of home oxygen therapy is changing the quality of life for COPD sufferers around the world.

Chronic obstructive pulmonary disease (COPD), which includes emphysema and chronic bronchitis, threatens the lives and futures of nearly 600 million people according to the World Health Organization. By 2020, COPD will become the third leading cause of death worldwide. Unfortunately, there is no cure. But there is hope and promising treatments. Clinicians have found that the use of supplemental home oxygen is one of the most effective new treatment options. In fact, long-term oxygen therapy has been shown to significantly improve life expectancy in patients with COPD.

But improved quality of life is equally important. Because COPD patients using home oxygen are relatively young, averaging between 45 and 60 years old, many find themselves juggling a job and children while coping with COPD. Meeting the demands of busy lives means today s COPD patients need a range of innovative devices that support both their health and lifestyles. To improve their quality of life, oxygen therapy must be smaller, lighter, longer-lasting, and highly portable. The ability to generate oxygen at home can also help patients avoid inconvenient waits for deliveries and better manage their time and therapy. COPD patients deserve solutions to address the health and quality of life challenges they face every day. Philips is leading the way in providing those solutions.

Home oxygen treatments designed for the front line

As a global leader in home healthcare, we are committed to the development of better home oxygen solutions to help people with chronic lung diseases such as COPD. At

Philips, what began with just one product in 2005 has now become a comprehensive portfolio of products, programs and services that is positively changing the way COPD patients live and work. With the launch of the HomeLox liquid oxygen system in June 2011, we reinforced our leadership position as the only manufacturer that offers a full line of supplemental oxygen devices for use in and out of the home.

But we realize that to truly improve the quality of life for COPD patients, our solutions have to address both the personal needs of patients and the business needs of homecare providers. Given the dramatic changes in healthcare delivery and costs over the past decade, Philips commitment to find innovative answers to the challenges of COPD means also creating a portfolio that reflects these challenging financial and market realities. By listening to our customers, we develop strong relationships that are helping us understand their unique challenges. Working together, we are able to better serve both patients and clinicians.

Having a manufacturer like Philips on our side is a game- changer. With reimbursements decreasing and competitive bidding on the rise, Philips helps us make good decisions. It s a great thing. because we can t do it alone, says customer Gordon Ridley, area manager, Petersen Medical.

The success of Philips home oxygen business shows in its outstanding financial performance. We tripled sales between 2005 and 2010, and success continued in 2011 with a double-digit annual growth rate.

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Global leadership through local relevance

With four regional product creation hubs leveraging the 2011 acquisitions of Preethi (India) and Povos (China), we are accelerating delivery of innovations that tap into the specific eating habits of different cultures around the world.

It s said that the two features that set a culture apart are the language its people speak and the food they eat. From soy milk makers in China to hand blenders with a cube cutter in Russia and mixer-grinders in India, we are building global leadership by delivering products that meet the needs of local populations.

The Kitchen Appliances market is big and growing, driven by demand in growth geographies, especially Asia. At the start of 2011 we moved the leadership of our Kitchen Appliances business to Shanghai. This way we are better positioned to pick up on local consumer insights and match our competitors time to market.

In record time

In China, sales of soy milk makers are booming due to consumers healthy lifestyles and an increasing desire to create soy milk at home from the bean, rather than buying the pre-made alternative. We acted upon this opportunity by accelerating our innovation process and delivering the first Philips soy milk maker to retailers in November.

We didn t just deliver a product to participate in this large market we also delivered meaningful innovation for consumers. New patents were filed for the easy filtering and anti-splash caps, and the product is the first on the market to use 100% food-grade lubricant in its motor. Initial consumer feedback has shown that consumers prefer Philips soy milk maker thanks to its design, its ease of cleaning and the smooth soy milk it makes thanks to its cutting and grinding performance.

Local salad-maker accessory speeds to market

Across Philips, we are focused on accelerating our performance to deliver more for customers. To achieve this, many teams are working to develop locally relevant and superior products and bring them to market faster. Created using local insights and by quickly developing a new and unique accessory for our flagship hand blender, the cube cutter developed for Russia and Eastern Europe is a great example of this.

Olivier salad, or Russian salad as it is often known outside the country where it was first created, is a popular dish composed of diced potatoes and other vegetables, as well as eggs and ham. It is one of the main courses served during Russian New Year celebrations, and as it is typically made in large quantities it takes a very long time to cube the vegetables during its preparation. This presented an opportunity to produce a dedicated cube cutter and save consumers the time and hassle of chopping manually with a knife.

Our market and business organizations worked closely together to develop an innovative solution to the problem, developing a dedicated cube-cutting accessory for the Philips Avance Collection hand blender. The team worked quickly, and as a result the product was on-shelf in Russian stores in time for the peak selling period in the run-up to the New Year celebrations. Localizing the product in time for this had an immediate positive effect on sales and market share.

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Building a global oral healthcare brand

With its range of Sonicare power toothbrushes Philips has pioneered innovation in oral healthcare and built up a loyal global following. Now we are expanding our global presence, broadening our portfolio and winning market share.

Through its Sonicare brand, Philips has a proven track record of driving growth in the power toothbrush market. That growth is driven by our innovation capability and the trust that dental professionals put in our products to improve their patients oral health. Today, we are expanding geographically into new markets, covering more price points and new channels. We are also expanding our portfolio through acquisitions and innovation to address more consumer needs, including new value spaces such as interdental cleaning.

Philips Sonicare the foundation of our oral healthcare business

Over 22 million enthusiastic users worldwide testify to the great experience of using Philips Sonicare toothbrushes. Pioneering sonic technology generates the brushes unique bristle-tip velocity a combination of high-frequency and high-amplitude bristle motions, delivering over 31,000 strokes per minute for an unrivalled cleaning experience.

A significant market that s set to grow

Around the world, 80% of people suffer from gingivitis. And in the West alone, 10-30% of people suffer from a periodontal disease. We estimate the addressable global market for oral healthcare at approximately EUR 50 billion, including consumables. Through our own innovations, alliances with dental professionals and acquisitions we are significantly increasing the proportion of the market that we address. At present, the market is concentrated in North America, Western Europe and Japan. The substantial growth of higher-income segments will drive growth in emerging markets. And as populations in developed markets continue to age, their oral healthcare needs will increase. And it s not just health concerns that are driving growth in the market consumers are increasingly turning to oral healthcare solutions that help them both look and feel good.

We can win in this market

In recent years we have seen good single-digit and now double-digit growth in oral healthcare. And the business is set to continue to grow faster than the market. We have strong relationships with dental professionals, who are key in driving consumer awareness of the benefits of good oral care.

We will drive growth by investing in innovation, branding and our relationships with dental professionals. We will expand into new channels such as online and pharmacies, and we will leverage Philips global market capabilities and make value-adding acquisitions. In 2010, for instance, we acquired the leading tooth-whitening firm Discus Dental, providing a strong foundation for growth in cosmetic dentistry and strengthening Philips position as a leading oral healthcare brand amongst dental professionals and consumers.

Innovations delivering clinically proven superiority

In 2011 we launched two of our most innovative product developments to date. Sonicare AirFloss is an easy, hassle- free alternative to regular flossing: its patented micro- burst technology releases a tiny burst of air and water between the teeth which removes 99% more plaque than brushing alone (with a manual toothbrush). And the Sonicare DiamondClean takes sonic tooth brushing to its most sophisticated level and provides the best clean yet, removing up to 100% of plaque from hard-to-reach places.

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Innovation bringing city lighting to life

CityTouch is an online outdoor lighting management system that enables dynamic, intelligent and flexible control city-wide. Combined with LED lighting, it can save up to 70% on energy and maintenance costs compared to conventional lighting.

With steeply rising urban populations, it is clear that static, passive streetlights simply can t keep up with the lives we lead. Truly livable cities require lighting that can adjust to the ebb and flow of traffic and urban activities. Drawing upon 120 years of experience in lighting innovation, we have created CityTouch providing the right amount of light precisely when and where it is needed.

Efficient, easy management

CityTouch enables users to manage all the lighting systems for an entire city from a single, intuitive online user interface. It provides easy, streamlined maintenance and oversight, with real-time status reports for each individual light point. That way, lighting operators can track the consumption and output of every part of their system and fine-tune lighting levels to meet local needs. Moreover, CityTouch helps cities face the dual challenge of cutting costs and protecting the environment. By making it possible to dim light points outside of peak hours, detect failures and provide smart lighting workflow support, the system significantly reduces operating costs and energy usage leading to lower energy bills, lower carbon emissions and less light pollution. CityTouch s asset management capabilities even cater for light points which are not connected, thereby significantly reducing maintenance and planning costs.

The case for LED lighting

Cities can maximize these savings by adopting energy- efficient LED lighting. Currently, lighting accounts for 19% of global electricity production. Around two thirds is based on energy-wasting technologies developed before 1970. A full switch to the latest LED lighting could lead to energy savings of up to 80% in many applications and reduce energy consumption for lighting by 40% worldwide. This equates to approximately EUR 130 billion per year in running costs and 670 million tons of avoided CO_2 emissions.

A future-proof solution

Lighting infrastructure represents a major investment for most cities, especially in times of constrained budgets. CityTouch protects that investment by adjusting seamlessly to new technologies and to the needs of our expanding cities. This is one of the system s greatest assets: that it is completely scalable and future-proof. As they grow, communities using CityTouch can simply add new streets and neighborhoods to the existing network. New lighting functionalities can easily be incorporated, and the underlying CityTouch service is continuously updated to meet new demands. Also, CityTouch is the first control platform that isn t bound to one hardware type or provider. This means that users have flexibility in choosing the products that best suit their city s requirements and budget secure in the knowledge that their light points will work seamlessly with the CityTouch system.

CityTouch is already being used by lighting operators in several European cities, including London and Prague. The London boroughs of Croydon and Lewisham, for example, are using CityTouch for a full PFI city lighting renovation project replacing more than 42,000 light points. CityTouch is empowering the lighting operator to adapt to the boroughs specific needs, providing both safety and flexibility while realizing significant savings on energy use and maintenance costs.

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Customer-centric innovation shaping the future of motoring

In the growth market of Daytime Running Lights, our Automotive business has shown it s got what it takes to Accelerate! by teaming up with its OEM and after-market customers, addressing their needs, and winning business.

The automotive lighting industry is undergoing radical transformation. More and more people are becoming mobile and want to stay mobile into old age. At the same time, there are growing legislative pressures, e.g. to reduce the environmental impact of motoring and to increase safety. Vehicle makers are also having to serve increasingly diverse needs, with consumer tastes ranging from functional economy cars to luxury vehicles. And new technologies such as our cutting-edge LED technology are changing the face of automotive design and performance.

We are getting closer to our automotive customers and taking ownership of their evolving lighting needs such as those arising from the recent European Union legislation making Daytime Running Lights (DRL) mandatory.

Advocating safer motoring

Automotive lighting is a major safety factor when driving: 40% of all accidents occur during the daytime. And 50% of these are caused by motorists failing to see another road user in time!

EU legislation stipulates that, as of 2011, all new passenger car models and small delivery vans must be equipped with DRL, with trucks and buses to follow in 2012. Through our insights and research activities we helped the EU reach its decision to adopt DRL. The introduction of DRL will make a positive contribution to our goal of reducing fatalities on European roads whilst being more fuel-efficient than existing lights, said Günter Verheugen, Vice President responsible for enterprise and industry policy.

Fast-growing market

With 20 million cars being produced in Europe each year, the EU-wide adoption of DRL represents a significant sales opportunity. It is expected that by 2015 40% of the European car park will be equipped with DRL (today 13%).

As well as selling to OEMs for build-in, we offer LED- based DRL solutions for cars already on the road, enabling drivers to benefit from the safety of DRL right now. Our LED Daylight retrofit modules enable lights to be switched on automatically when the engine is started. These lights substantially increase a car s visibility to other road users and have a low energy consumption compared to existing dipped-beam headlamps. LED DayLight 4 ensures high visibility for safer daytime driving, while LED DayLight 8 offers motorists maximum visibility and premium design. Both enable CO2 savings of 5.5 g per km, while their long lifetime significantly reduces the need for maintenance.

Safety, energy efficiency and style

As the world s leading automotive lighting player, we are committed to understanding our customers needs and helping them to enhance the motoring experience with innovations that make their vehicles safer, more energy- efficient and more stylish. A fact not lost on Mercedes-Benz: We have chosen Philips as our partner for the next-generation LED DRLs, says Uwe Kostanzer, head of Mercedes-Benz s exterior lighting department, not only due to the product s supremacy in lumen output, quality of light and thermal stability, but also due to the entirely trustful cooperation between the engineering teams on both sides.

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4 Our planet, our partners, our people

Optimizing our ecological footprint

Responsible corporations are taking decisive action to fight climate change and increase resource efficiency. And Philips is leading the way.

To help reduce global CO_2 emissions, companies can either focus on their own operations, for example by reducing energy and material consumption in their activities. Or, they can focus on making their products more ecologically efficient. At Philips we focus on both and much more.

The key performance indicators of our EcoVision program reflect our holistic approach to sustainability. Two of these focus on optimizing our ecological footprint, namely energy efficiency and materials .

Recognition of leadership

At all levels of our operations in 2011, we continued to monitor and minimize the CO2 emissions resulting from our activities. As a result, in September, the independent not-for-profit organization Carbon Disclosure Project (CDP) awarded us the top score of 99 (out of 100) for Carbon Disclosure and an A for our overall Carbon Performance.

Our sustainability performance in 2011 also led to us regaining our sector and super-sector leadership in the Dow Jones Sustainability Index.

Green Products and Green Innovation

In 2011 we continued our drive for Green Products new products that are significantly better (by at least 10%) than either their Philips predecessor or their nearest competitor. Six specific areas are considered in the Green Product classification process: energy efficiency, packaging, hazardous substances, weight, recycling & disposal, and lifetime reliability.

One of the sustainability product highlights in 2011, addressing the subject of materials, was our launch of the world s first ever recycled designer coffee machine: the SENSEO Viva Café Eco, which uses old electronic appliances to create a first-class coffee system. All outer plastic parts except those that come into contact with the water or coffee are made from up to 100% recycled content. The machine also has a five-minute auto shut- off for energy saving, and its packaging is made from 90% recycled cardboard.

Also last year, after 18 months of rigorous testing, the US Department of Energy awarded us the highly prestigious L Prize for our LED replacement for the 60 W incandescent bulb. The Department calculated that if every 60 W incandescent bulb in the US was replaced with our 10 W prize winner, the nation would save USD 3.9 billion in one year and avoid 20 million tons of carbon emissions. This is comparable with the emission reduction that could be realized by shutting down 20 medium-size power stations.

Our InteliVue MX40 Patient Monitor and Trilogy home healthcare solution illustrate how our innovations are also significantly reducing energy usage in the hospital and home settings.

And to ensure our green pipeline remains well stocked, we invested some EUR 470 million in Green Innovation in 2011.

Greener business models

We are also creating innovative new business models that help improve our ecological footprint. For example, the Pay per Lux lighting concept currently being trialed in the Netherlands provides companies with energy-saving, state-of-the-art lighting systems without any capital expenditure. It works like this: after installation, we retain ownership and maintenance of the lighting, and in return the customer pays only for the amount of light emitted. This encourages the deployment of energy-efficient products and advanced lighting controls.

Partnering to drive change

In addition to our own sustainability activities, we also influence those of our supply chain partners, both up- and down-stream from our activities. This helps ensure the broadest possible impact for positive change.

In recognition of our efforts in the area of responsible supply chain management, the Dutch Association of Investors for Sustainable Development (VBDO) ranked us first among 40 of the largest publicly-listed companies in the Netherlands. Our scores have shown continual improvement over the last five years, rising from 62% in 2006 to 93% in 2010, and the highest score ever of 95% in 2011. In particular, VBDO praised the transparency and openness of our sustainability programs related to our supply chains, as well as our enhanced engagement in helping our suppliers to improve their sustainability performance.

Partnership organizations

Besides working with our supply chain partners, we are an active member of several initiatives implementing industry-wide sustainability programs.

For example, we are a member of the Electronic Industry Citizenship Coalition (EICC), which promotes an industry code of conduct to improve working and environmental conditions within global supply chains. Today, the EICC includes more than 50 global electronics companies and their suppliers.

We are also one of the initiators of the IDH Electronics Program, a multi-stakeholder initiative sponsored by the Sustainable Trade Initiative (IDH) together with Dell, Hewlett-Packard, and civil society organizations. This program will work with over 100 electronics suppliers in China to support innovative workforce management practices, sustainability and better business performance. The goal is to improve working conditions of more than 500,000 employees in the electronics sector.

The first phase of the program started in November 2011, with four of our suppliers joining. Each supplier receives support over a period of up to 24 months on the basis of improved dialogue between management and workers. The costs of the program are shared between the supplier, its customer, and the IDH.

Effective partnering

In November 2011 we announced, together with South African public utility Eskom, the largest energy-saving LED lighting deal in Africa to date. Some 200,000 of our MASTER LED lamps will be distributed at discounted prices throughout South Africa s hotels, banks, offices and retail outlets. Because the 7 and 10 W LED lamps replace 50 W halogens, the annual CO2 reduction will be 60,000 tons. And all it takes is the simple replacement of a bulb!

In 2011 we were also praised, along with The Climate Group, for our solar-driven LED street-lighting project in China s Guiyang community. The UN s Momentum for Change event cited the project as a best practice example of public-private partnership that enhances people s lives in poor rural communities, while spurring green growth, saving energy and combating climate change.

Also, for the second year running we worked with Oxfam Novib and electrical distributor Sonepar on a special LED promotion in Uganda on solar-lighting solutions to stimulate education after dark. By using our simple, LED- based solar lighting solutions, thousands of children in off-grid areas can now do their homework in the evenings. And communities in general can benefit from safe, sustainable and clean lighting.

Our people making a difference

Philips employees are the key enabler for making a difference, both within the company and to the lives of people we touch with our meaningful innovations and community programs.

Through the Accelerate! program, Philips is addressing structural change, focusing on execution, reducing overhead costs, investing in growth and adopting a new company culture. This cultural shift is being driven by a new set of behaviors designed to help us unlock our full potential *Eager to win, Take ownership* and *Team up to excel.*

Bringing care to people

At Philips, we are dedicated to making a difference wherever care is provided. In the hospital setting that means supporting and enabling the delivery of critical care, emergency care and surgery. With chronic disease on the rise, the home setting will play an increasingly prominent role in the delivery of care moving forward. Our oral healthcare, light therapy, water purification and air purification products, as well as our solar-powered indoor lamps replacing kerosene lamps in Africa these are just some of the examples of how we bring care to people. Progress on this social dimension of our EcoVision program is measured by the number of lives we touch. Through our products and solutions for bringing care to people we touched 465 million lives in 2011, an increase of 45 million compared to 2010.

Community engagement

In parallel to our daily business focus on customers and markets, we also continue to encourage our people to engage with their immediate wider community. As part of our commitment to sustainability, Philips supports volunteer activities as a way of giving back to our communities. Employee volunteering embraces Philips mission to improve people s lives not only through our technical innovations, but also through our employees and our shared belief that each of us can touch the lives of those around us, making our world a better place.

Our behaviors

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A key initiative in this respect is our SimplyHealthy@Schools program. Across the globe, Philips employees have volunteered to upgrade lighting in local schools and educate the children on energy efficiency. But the program goes much further. The SimplyHealthy@Schools Healthy Heroes toolkit is aimed at children aged 8-12 years and illustrates simple ways of improving health and well-being by paying attention to air, light, water, sleep and oral hygiene, as well as to exercise and care for the environment. When these factors are addressed, children perform better and their overall mental and physical well-being improves.

New volunteering program in the USA

In 2011 we also launched a new employee volunteer program in North America called Philips Cares: giving back to our communities . Philips Cares utilizes an online portal in conjunction with relationships with non-profit organizations across the United States to provide employees with the opportunity to participate in meaningful volunteer opportunities that suit their individual needs, schedule and passion. Since the program launched, thousands of employees have taken action to give back to their community. Examples include a Build-a- Bike event in Salina, Kansas, a Charity Chili Cook-off in Tupelo, Mississippi, and a Day of Caring event in Bothell, Washington.

5 Group performance

2011 was a challenging year in terms of Philips financial performance. The macro-economic developments and the weakness of the Western European markets further impacted this. Despite the challenges we achieved 4% comparable sales growth at the lower end of our mid-term performance bandwidth, with a strong contribution from growth geographies (33% of sales) and 7.4% Adjusted IFO margin.

Ron Wirahadiraksa, Chief Financial Officer

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5 Group performance 5.1 - 5.1

5.1 Management discussion and analysis

Prior years results and cash flows have been restated to reflect the effect of classifying the Television business as discontinued operations in 2011.

Management summary

Key data

in millions of euros unless otherwise stated

	2009	2010	2011
Sales	20,092	22,287	22,579
Adjusted IFO[1]	1,096	2,562	1,680
as a % of sales	5.5	11.5	7.4
IFO	660	2,080	(269)
as a % of sales	3.3	9.3	(1.2)
Financial income and expenses	(162)	(121)	(240)
Income tax expense	(99)	(499)	(283)
Results of investments in associates	77	18	16
Income (loss) from continuing operations	476	1,478	(776)
Income (loss) from discontinued operations	(52)	(26)	(515)
Net income (loss)	424	1,452	(1,291)
Net income (loss):			
Per common share basic	0.46	1.54	(1.36)
Per common share diluted	0.46	1.53	(1.36)
Net operating capital (NOC)[1]	12,649	11,951	10,427
Cash flows before financing activities[1]	1,226	1,475	(528)
Employees (FTEs)[2]	116,153	119,775	125,241
of which discontinued operations	4,764	3,610	3,353

1) For a reconciliation to the most directly comparable GAAP measures, see chapter 15, Reconciliation of non-GAAP information, of this report
2) Adjusted to reflect a change of employees reported in the Healthcare sector for the past periods

The year 2011

2011 was a challenging year for Philips, in which financial performance was impacted by overall market weakness, particularly in Western Europe towards the end of the year. We recorded 4% comparable sales growth, with a strong contribution from growth geographies, while largely as a result of continued investments for growth, gross margin pressure and goodwill impairments we saw earnings decline compared to the previous year. The net loss for the year amounted to EUR 1,291 million, which was mainly attributable to lower earnings, impairment charges in the second quarter of the year and costs related to the discontinued operations of the Television business as a result of the signing of a joint venture agreement with TPV.

Sales amounted to EUR 22.6 billion, a 1% nominal increase for the year. Excluding unfavorable currency effects and portfolio changes, comparable sales were 4% above 2010. Comparable sales growth was driven by Lighting and Healthcare, while Consumer Lifestyle sales were in line with the previous year. Within Lighting, strong growth was seen in the Professional Luminaires business, mainly fueled by the construction market in growth geographies, and the Lamps business, partly mitigated by a sales decline at Lumileds. Healthcare sales grew 5%, with solid growth in all businesses, particularly Patient Care & Clinical Informatics. Sales at Consumer Lifestyle were in line with 2010, but showed an improvement in the second part of the year, where strong growth at Health & Wellness, Personal Care and Domestic Appliances was tempered by a sales decline in our Lifestyle Entertainment business.

Our growth geographies achieved comparable 11% growth, while mature geographies grew by a modest 1%, as a result of the overall macro-economic developments and weakness of the Western European markets. In 2011 growth geographies accounted for 33% of total sales, compared to 31% in 2010.

IFO amounted to a loss of EUR 269 million, or minus 1.2% of sales, compared to EUR 2,080 million, or 9.3% of sales, in 2010. IFO decline was mainly seen at Lighting and Healthcare, largely as a result of EUR 1,355 million of goodwill impairment charges taken in the second quarter of 2011, as well as lower operational earnings in all sectors. The latter was mainly due to continued pressures on gross margin, reflecting challenging economic conditions as well as higher investments for future growth.

We continued to invest in strategically aligned companies, primarily to strengthen our product portfolio in growth geographies. In 2011, we completed six acquisitions, contributing to all three sectors, notably Preethi and Povos in Consumer Lifestyle and Sectra in Healthcare. The cash outflow related to acquisitions amounted to EUR 552 million.

In 2011 we generated EUR 836 million of cash flow from operating activities, which was EUR 1,285 million lower than in 2010. The decline was largely a result of the lower cash earnings and higher working capital requirements mainly related to tightening the accounts payable procedures and the timing of tax payable, which was partly mitigated by lower inventory build. Our cash flows before financing activities were EUR 2,003 million below the level of 2010, due to lower cash flow from operating activities, lower proceeds from the sale of stakes and interests, and higher outflow related to acquisitions of new businesses and capital expenditures.

In July 2011 we launched a EUR 2 billion share buy- back program aimed at improving the efficiency of our balance sheet. By the end of the year we had completed 35% of this program.

The year 2010

In 2010, despite experiencing a recovery in certain markets, overall worldwide market conditions remained challenging, particularly in developed countries. We recorded 5% comparable sales growth.

IFO of EUR 2,080 million, or 9.3% of sales, was significantly higher than the EUR 660 million, or 3.3% of sales, achieved in 2009. Significant IFO improvement, led by Lighting, was achieved in all sectors.

Following a strong rebound in the first six months of the year, sales growth slowed in the second half, ending at 11% nominal for the full year. Adjusted for favorable currency effects, comparable sales were 5% higher than in 2009, attributable to growth in all sectors, notably Lighting. Within Lighting, growth in automotive and LED markets was strong, partly mitigated by limited growth at Professional Luminaires due to weak construction markets in the US and Western Europe; Healthcare sales grew 4%, supported by 6% growth in all businesses except Imaging Systems, which was broadly in line with 2009. Growth at Consumer Lifestyle was limited to 1%, as solid growth at Health & Wellness and Personal Care was tempered by a sales declines at Lifestyle Entertainment.

14% comparable sales growth was achieved in growth geographies, while mature geographies grew 1%. Growth geographies accounted for 31% of total sales, up from 30% in 2009.

In 2010, we completed 11 acquisitions, contributing to all three sectors, notably Discus Holdings in Consumer Lifestyle. The cash outflow related to acquisitions amounted to EUR 241 million.

We generated EUR 2.1 billion of cash flow from operating activities, EUR 730 million higher than in 2009. Our cash flows before financing activities were EUR 249 million higher than 2009, as higher cash flow from operating activities was partly offset by lower proceeds from the sale of stakes.

5.1.1 Sales

The year 2011

The composition of sales growth in percentage terms in 2011, compared to 2010, is presented in the table below.

Sales growth composition 2011 versus 2010

in %

	comparable growth	currency effects	consolidation changes	nominal growth
Healthcare	5.3	(2.5)	0.1	2.9
Consumer Lifestyle	(0.1)	(1.7)	2.6	0.8
Lighting	6.1	(2.3)	(2.7)	1.1
GM&S	2.4		(28.3)	(25.9)

Philips Group	4.1	(2.2)	(0.6)	1.3

Group sales amounted to EUR 22,579 million in 2011, representing 1% nominal growth compared to 2010. Adjusting for a 2% unfavorable currency effect and a 1% unfavorable portfolio effect, comparable sales were 4% above 2010. Comparable sales were 6% higher at Lighting and 5% higher at Healthcare, but this was tempered by Consumer Lifestyle, where sales were broadly in line with the previous year.

Healthcare sales amounted to EUR 8,852 million, which was 5% higher than in 2010 on a comparable basis. Higher sales were driven by mid-single-digit growth at all businesses, as increases in growth geographies and North America were partially offset by lower sales in Western Europe.

Consumer Lifestyle reported sales of EUR 5,823 million, which was EUR 48 million higher than in 2010, or flat on a comparable basis. We achieved double-digit growth at Health & Wellness and high single-digit growth at Personal Care and Domestic Appliances. This was offset by a sales decline at Lifestyle Entertainment.

Lighting sales amounted to EUR 7,638 million, which was EUR 86 million higher than in 2010, or 6% higher on a comparable basis. Growth was largely driven by high single digit growth at Professional Luminaires, Lighting Systems & Controls and Lamps. This was tempered by sales declines at Lumileds and Consumer Luminaires.

GM&S reported sales of EUR 266 million, which was EUR 93 million lower than in 2010, mainly due to the divestment of Assembléon in the first quarter of 2011. Excluding Assembléon and other portfolio changes, sales were 2% higher than in 2010 on a comparable basis, attributable to higher license income.

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The year 2010

The composition of sales growth in percentage terms in 2010, compared to 2009, is presented in the table below.

Sales growth composition 2010 versus 2009

in %

	comparable growth	currency effects	consolidation changes	nominal growth
Healthcare	3.9	6.0	(0.2)	9.7
Consumer Lifestyle	1.3	4.8	1.4	7.5
Lighting	8.7	6.0	0.7	15.4
GM&S	6.4	2.7	(2.6)	6.5
Philips Group	4.8	5.6	0.5	10.9

Group sales amounted to EUR 22,287 million in 2010, 11% nominal growth compared to 2009. Excluding a 6% favorable currency effect, comparable sales were 5% above 2009. Comparable sales were 9% higher at Lighting and 4% higher at Healthcare, though were tempered by 1% higher sales at Consumer Lifestyle.

Healthcare sales amounted to EUR 8,601 million, which was 4% higher than in 2009 on a comparable basis, driven by 6% growth at Patient Care & Clinical Informatics, Home Healthcare Solutions, and Customer Services. Sales at Imaging Systems were broadly in line with 2009, as increase in growth geographies was largely offset by lower sales in North America.

Consumer Lifestyle reported sales of EUR 5,775 million, which was EUR 405 million higher than in 2009, or 1% higher on a comparable basis. We achieved double-digit growth at Health & Wellness and high single-digit growth at Personal Care. This was tempered by a year-on-year sales declines at Lifestyle Entertainment.

Lighting sales amounted to EUR 7,552 million, which was EUR 1 billion higher than in 2009, or 9% higher on a comparable basis. Growth was largely driven by double- digit growth at Lumileds, Automotive Lighting, and Lighting Systems & Controls. Ongoing weakness in residential and commercial construction markets meant our Luminaires businesses yielded little growth.

5.1.2 Earnings

The year 2011

In 2011, Philips gross margin was EUR 8,647 million, or 38.3% of sales, compared to EUR 9,096 million, or 40.8% of sales, in 2010. Gross margin in 2011 was impacted by a EUR 128 million charge related to the impairment of customer relationships and brand names in Consumer Luminaires, as well as raw material price increases. Gross margin in 2011 included EUR 53 million in restructuring and acquisition-related charges, whereas 2010 included EUR 97 million in restructuring and acquisition-related charges. Gross margin percentage was lower than in 2010 for all sectors, notably Lighting and Consumer Lifestyle.

Selling expenses increased from EUR 4,876 million in 2010 to EUR 5,160 million in 2011. 2011 included EUR 54 million in restructuring and acquisition-related charges, compared to EUR 75 million in 2010. The year-on-year increase was mainly attributable to higher expenses aimed at driving higher market penetration and increased spending on advertising and promotion. In relation to sales, selling expenses increased from 21.9% to 22.9%. Compared to 2010 selling expenses as a percentage of sales declined in Healthcare, while they were higher in Lighting and Consumer Lifestyle.

General and administrative expenses amounted to EUR 841 million in 2011, compared to EUR 713 million in 2010. In 2010, general and administrative expenses included a EUR 119 million gain related to a change in pension plan, compared to a gain of EUR 21 million in 2011. As a percentage of sales, costs increased from 3.2% in 2010 to 3.7%.

Research and development costs increased from EUR 1,493 million in 2010 to EUR 1,610 million in 2011. The year-on-year increase was largely attributable to higher investments in innovation to support growth. As a percentage of sales, research and development costs increased from 6.7% in 2010 to 7.1%.

The overview below shows sales, IFO and Adjusted IFO according to the 2011 sector classifications.

Sales, IFO and Adjusted IFO 2011

in millions of euros unless otherwise stated

	sales	IFO	%	Adjusted IFO[1]	%
Healthcare	8,852	93	1.1	1,145	12.9
Consumer Lifestyle	5,823	392	6.7	472	8.1
Lighting	7,638	(362)	(4.7)	445	5.8
GM&S	266	(392)		(382)	
Philips Group	22,579	(269)	(1.2)	1,680	7.4

1) For a reconciliation to the most directly comparable GAAP measures, see chapter 15, Reconciliation of non-GAAP information, of this report

Sales, IFO and Adjusted IFO 2010

in millions of euros unless otherwise stated

	sales	IFO	%	Adjusted IFO[1)]	%
Healthcare	8,601	922	10.7	1,186	13.8
Consumer Lifestyle	5,775	679	11.8	718	12.4
Lighting	7,552	695	9.2	869	11.5
GM&S	359	(216)		(211)	
Philips Group	22,287	2,080	9.3	2,562	11.5

1) For a reconciliation to the most directly comparable GAAP measures, see chapter 15, Reconciliation of non-GAAP information, of this report

In 2011, IFO decreased by EUR 2,349 million compared to 2010, to a loss of EUR 269 million, or minus 1.2% of sales. 2011 included EUR 163 million in restructuring and acquisition-related charges, compared to EUR 203 million in 2010. The year-on-year decrease was mainly driven by goodwill impairments of EUR 1,355 million, lower gross margin percentages in Lighting and Consumer Lifestyle, and lower IFO in Group Management & Services.

Amortization of intangibles, excluding software, capitalized product development and impairment- related charges, amounted to EUR 594 million in 2011, compared to EUR 482 million in 2010.

Adjusted IFO decreased from EUR 2,562 million, or 11.5% of sales, in 2010 to EUR 1,680 million, or 7.4% of sales, in 2011. The decrease in Adjusted IFO was attributable to all sectors.

Healthcare

Adjusted IFO decreased from EUR 1,186 million, or 13.8% of sales, in 2010 to EUR 1,145 million, or 12.9% of sales, in 2011. Adjusted IFO improved in Customer Services, Home Healthcare Solutions and PCCI, but was more than offset by lower results in Imaging Systems. Restructuring and acquisition-related charges totaled EUR 20 million, compared to EUR 77 million in 2010.

Consumer Lifestyle

Adjusted IFO decreased from EUR 718 million, or 12.4% of sales, in 2010 to EUR 472 million, or 8.1% of sales, in 2011. Restructuring and acquisition-related charges amounted to EUR 54 million in 2011, compared to EUR 31 million in 2010. The year-on-year Adjusted IFO decrease was largely due to lower sales, particularly in Lifestyle Entertainment, higher investments in advertising and promotion, as well as lower license income. Adjusted IFO was higher than in 2010 in Health & Wellness, while in all other businesses it declined.

Lighting

Adjusted IFO decreased from EUR 869 million, or 11.5% of sales, in 2010 to EUR 445 million, or 5.8% of sales, in 2011. Restructuring and acquisition-related charges amounted to EUR 66 million in 2011, compared to EUR 97 million in 2010. The decrease in Adjusted IFO was largely attributable to lower gross margin due to raw material price increases, as well as step-ups in investments related to growth.

Group Management & Services

Adjusted IFO decreased from a loss of EUR 211 million in 2010 to a loss of EUR 382 million in 2011. Adjusted IFO in 2010 included a EUR 119 million gain related to a change in pension plan. 2011 results included a EUR 21 million gain from a change in a pension plan, and EUR 23 million in restructuring charges. The year-on-year Adjusted IFO decrease was largely attributable to higher pension costs, provisions for legal and environmental claims, and investments related to the Accelerate! program.

For further information regarding the performance of the sectors, see chapter 6, Sector performance, of this report.

The year 2010

In 2010, Philips gross margin was EUR 9,096 million, or 40.8% of sales, compared to EUR 7,573 million, or 37.7% of sales, in 2009. Gross margin in 2010 included EUR 96 million restructuring and acquisition-related charges, whereas 2009 included EUR 223 million of restructuring and acquisition-related charges and net asbestos-related recoveries of EUR 57 million. Gross margin percentage was higher than in 2009 in all operating sectors, notably Lighting.

Selling expenses increased from EUR 4,703 million in 2009 to EUR 4,876 million in 2010. 2010 included EUR 75 million of restructuring and acquisition-related charges, compared to EUR 158 million in 2009. The year-on-year increase was mainly attributable to higher expenses aimed at supporting higher sales, and increased investments in advertising and promotion. In relation to sales, selling expenses decreased from 23.4% in 2009 to 21.9% in 2010. Expenses were lower than in 2009 in all sectors.

General and administrative expenses amounted to EUR 713 million in 2010, compared to EUR 721 million in 2009. As a percentage of sales, costs improved from 3.6% in 2009 to 3.2% in 2010.

Research and development costs declined from EUR 1,542 million in 2009 to EUR 1,493 million in 2010. The year-on-year decline was largely attributable to lower restructuring and acquisition-related charges, which amounted to EUR 10 million in 2010, compared to EUR 68 million in 2009, and to the discontinuation of certain activities in the field of Molecular Healthcare and 3D Displays. As a percentage of sales, research and development costs decreased from 7.7% in 2009 to 6.7% in 2010.

The overview above shows sales, IFO and Adjusted IFO according to the 2010 sector classifications.

Sales, IFO and Adjusted IFO 2009

in millions of euros unless otherwise stated

	sales	IFO	%	Adjusted IFO[1)]	%
Healthcare	7,839	593	7.6	848	10.8
Consumer Lifestyle	5,370	436	8.1	454	8.5
Lighting	6,546	(16)	(0.2)	145	2.2
GM&S	337	(353)		(351)	
Philips Group	20,092	660	3.3	1,096	5.5

1) For a reconciliation to the most directly comparable GAAP measures, see chapter 15, Reconciliation of non-GAAP information, of this report

In 2010, IFO increased by EUR 1,420 million compared to 2009, to EUR 2,080 million, or 9.3% of sales. 2010 included EUR 203 million of restructuring and acquisition-related charges, compared to EUR 489 million in 2009. In addition to lower restructuring and acquisition-related charges, the year-on-year improvement was mainly driven by higher sales and a higher gross margin percentage in each of the operating sectors, and lower costs in Group Management & Services.

Amortization of intangibles, excluding software and capitalized product development, amounted to EUR 487 million in 2010, compared to EUR 436 million in 2009. Amortization charges were higher than in 2009 due to acquisitions.

Adjusted IFO increased from EUR 1,096 million, or 5.5% of sales, in 2009 to EUR 2,562 million, or 11.5% of sales, in 2010. Higher Adjusted IFO was visible in all sectors, notably Lighting.

Healthcare

Adjusted IFO increased from EUR 848 million, or 10.8% of sales, in 2009 to EUR 1,186 million, or 13.8% of sales, in 2010. Adjusted IFO improvements were realized across all businesses, largely as a result of higher sales, favorable currency impact and cost-saving programs. Restructuring and acquisition-related charges totaled EUR 77 million, compared to EUR 106 million in 2009.

Consumer Lifestyle

Adjusted IFO improved from EUR 454 million, or 8.5% of sales, in 2009 to EUR 718 million, or 12.4% of sales, in 2010. Restructuring and acquisition-related charges amounted to EUR 31 million in 2010, compared to EUR 74 million in 2009. The year-on-year Adjusted IFO improvement was largely driven by higher sales, fixed cost savings, EUR 48 million product recall related charges in 2009, and lower restructuring charges. Adjusted IFO was higher than in 2009 in all businesses. Notable improvements were achieved in Domestic Appliances and Licenses.

Lighting

Adjusted IFO amounted to EUR 869 million, or 11.5% of sales, which included EUR 97 million of restructuring and acquisition-related charges. EUR 247 million of restructuring and acquisition-related charges were included in 2009. The Adjusted IFO improvement was also driven by higher sales, improved gross margin and fixed cost savings from restructuring programs.

Group Management & Services

Adjusted IFO improved from a loss of EUR 351 million in 2009 to a loss of EUR 211 million in 2010. 2010 results included a EUR 119 million gain from a change in a pension plan. Adjusted IFO in 2009 included a EUR 134 million gain related to curtailment for retiree medical benefit plans, EUR 57 million of net asbestos-related recoveries, and EUR 46 million of asset write-offs. 2009 also included EUR 63 million restructuring charges. The year-on-year Adjusted IFO improvement was largely attributable to higher license revenue, discontinuation of Molecular Healthcare, and lower costs in the global service units.

5.1.3 Pensions

The year 2011

The net periodic pension costs of defined-benefit pension plans amounted to a cost of EUR 18 million in 2011, compared to a credit of EUR 105 million in 2010. The defined-contribution pension cost amounted to EUR 120 million, EUR 6 million higher than in 2010.

In 2011, further steps were taken to manage the financial exposure to defined benefit plans. One of our major plans was frozen and the active members were transferred to a defined contribution plan, causing a curtailment gain. In the same plan, a prior-service gain was recognized due to retired members opting for a one-off benefit increase in exchange for future indexation. The overall curtailment gain for 2011 was EUR 18 million and the prior-service cost gain was EUR 20 million.

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The funded status of our defined benefit plans deteriorated in 2011 due to adverse market movements and lower interest rates. However, this was largely offset by the unrecognized surpluses of the Group s main plans, reducing the impact on the net balance sheet position.

In 2010, results were positively impacted by the recognition of EUR 119 million of negative prior-service costs. These resulted from a reduction of pension benefits expected to be paid in the future, in part due to a change in indexation. In 2010, a curtailment gain of EUR 9 million on one of our retiree medical plans was recognized due to the partial closure of a US site.

For further information, refer to note 29, Pensions and other postretirement benefits.

The year 2010

The net periodic pension costs of defined-benefit pension plans amounted to a credit of EUR 105 million in 2010, compared to a net result of 0 in 2009. The defined- contribution pension cost amounted to EUR 114 million, EUR 11 million higher than in 2009, mainly due to a gradual shift from defined-benefit to defined-contribution pension plans.

The 2010 costs were impacted by the recognition of EUR 119 million of negative prior-service costs. These resulted from a reduction of pension benefits expected to be paid in the future, in part due to a change in indexation. In 2010, a curtailment gain of EUR 9 million on one of our retiree medical plans was recognized due to the partial closure of a US site.

In 2009, curtailment gains totaling EUR 134 million, relating to changes in retiree medical plans, positively impacted the result. These curtailment gains are the result of changes in the benefit level and the scope of eligible participants of a retiree medical plan, which became effective and irreversible in 2009.

For further information, reference is made to note 29, Pensions and other postretirement benefits.

5.1.4 Restructuring and impairment charges

The year 2011

In 2011, IFO included net charges totaling EUR 1,572 million for restructuring and related asset impairments. The annual impairment test led to selected adjustments of pre-recession business cases as well as an adjustment of the discount rate across Philips, leading to a EUR 1,355 million impairment of goodwill. In addition to the annual goodwill impairment tests, trigger-based impairment tests were performed during the year, but resulted in no further goodwill impairments. 2011 also included a EUR 128 million charge related to the impairment of customer relationships and brand names at Consumer Luminaires.

2010 included EUR 132 million in restructuring and related asset impairment charges.

For further information on sensitivity analysis, please refer to note 9, Goodwill.

Restructuring and related charges

in millions of euros

	2009	2010	2011
Restructuring and related charges per sector:			
Healthcare	42	48	3
Consumer Lifestyle	57	12	9
Lighting	225	74	54

Group Management & Services	63	(2)	23
Continuing operations	387	132	89
Discontinued operations	63	30	15
Cost breakdown of restructuring and related charges:			
Personnel lay-off costs	331	151	109
Release of provision	(66)	(70)	(45)
Restructuring-related asset impairment	81	14	10
Other restructuring-related costs	41	37	15
Continuing operations	387	132	89
Discontinued operations	63	30	15

In 2011, the most significant restructuring projects related to Lighting and Group Management & Services and were mainly driven by our change program Accelerate!. Restructuring projects at Lighting centered on Luminaires businesses and Lamps, the largest of which took place in the Netherlands, Brazil and in the US. Group Management & Services restructuring projects focused on the Global Service Units (primarily in the Netherlands), Corporate and Country Overheads (mainly in the Netherlands, Brazil and Italy) and Philips Design (the Netherlands). In Healthcare, the largest projects were undertaken in Imaging Systems, Home Healthcare Solutions and Patient Care & Clinical Informatics in various locations in the US to reduce the operating costs and simplify the organization. Consumer Lifestyle restructuring charges mainly related to our remaining Television operations in Europe.

The restructuring charges in 2010 were mainly attributable to the operating sectors. Within Healthcare, the largest projects related to the reorganization of the commercial organization in Imaging Systems (Germany, the Netherlands and the US). Consumer Lifestyle restructuring charges were mainly in Lifestyle Entertainment, primarily in the Netherlands and the US. Restructuring projects in Lighting were focused on the reduction of production capacity in traditional lighting technologies, such as incandescent. The largest projects were initiated in Brazil, France and the US.

For further information on restructuring, refer to note 20, Provisions.

The year 2010

In 2010, IFO included net charges totaling EUR 132 million for restructuring and related asset impairments. 2009 included EUR 387 million of restructuring and related asset impairment charges. In addition to the annual goodwill impairment tests for Philips, trigger-based impairment tests were performed during the year, resulting in no goodwill impairments.

For further information on sensitivity analysis, please refer to note 9, Goodwill.

The restructuring charges in 2010 were mainly attributable to the operating sectors. Within Healthcare, the largest projects related to the reorganization of the commercial organization in Imaging Systems (Germany, Netherlands, and the US). Consumer Lifestyle restructuring charges were mainly in Lifestyle Entertainment, primarily in the Netherlands and the US. Restructuring projects in Lighting were focused on reduction of production capacity in traditional lighting technologies, such as incandescent. The largest projects were initiated in Brazil, France, and the US.

In 2009, the most significant restructuring projects related to Lighting and Consumer Lifestyle. Restructuring projects at Lighting centered on Lamps. The largest restructuring projects were in the Netherlands, Belgium, Poland and various locations in the US. Consumer Lifestyle restructuring projects focused on Lifestyle Entertainment (mainly Technology & Development in the Netherlands) and Domestic Appliances (mainly Singapore and China). Healthcare initiated various restructuring projects aimed at reduction of the fixed cost structure, mainly impacting Imaging Systems (Netherlands), Home Healthcare Solutions and Patient Care & Clinical Informatics (various locations in the US).

Other restructuring projects focused on reducing the fixed cost structure of Corporate Technologies, Philips Information Technology, Philips Design, and Corporate Overheads within Group Management & Services.

Reference is made to note 20, Provisions. For further information on impairment please refer to the information under the heading Impairment of non- financial assets in section 5.7, Critical accounting policies, of this report.

5.1.5 Financial income and expenses

The year 2011

A breakdown of Financial income and expenses is presented in the table below.

Financial income and expenses

in millions of euros

	2009	2010	2011
Interest expense (net)	(252)	(225)	(210)
Sale of securities	126	162	51
Impairment on securities	(58)	(2)	(34)
Other	22	(56)	(47)

	(162)	(121)	(240)

The net interest expense in 2011 was EUR 15 million lower than in 2010, mainly as a result of lower average outstanding debt.

Sale of securities

in millions of euros

	2009	2010	2011
Gain on sale of NXP shares		154	
Gain on sale of TCL shares			44
Gain on sale of LG Display shares	69		
Gain on sale of Digimarc shares			6
Gain on sale of Pace shares	48		
Others	9	8	1
	126	162	51

In 2011, income from the sale of securities totaled EUR 51 million. This included a EUR 44 million gain from the sale of the remaining shares in TCL and a EUR 6 million gain on the sale of shares of Digimarc. In 2010, income from the sale of securities of EUR 162 million was mainly attributable to the sale of NXP shares.

Impairments on securities

in millions of euros

	2009	2010	2011
NXP	(48)		
TPV			(25)
Chi-Mei Innolux			(4)
BG Medicine			(2)
Prime Technology	(6)	(2)	(1)
Other	(4)		(2)
	(58)	(2)	(34)

2011 was impacted by impairment charges amounting to EUR 34 million, mainly from shareholdings in TPV Technologies Ltd.

Other financial expenses totaled to a EUR 47 million expense in 2011, compared to EUR 56 million in 2010. In 2011 these primarily consisted of a EUR 35 million other financing charge and a EUR 33 million accretion expense (mainly associated with discounted provisions) offset by EUR 11 million dividend income and other financial income, including a net gain of EUR 6 million mostly from the revaluation impact of the option related to NXP.

Other financial expenses in 2010 primarily consisted of a EUR 21 million expense related to the revaluation of the convertible bonds received from TPV Technology and CBAY, and a EUR 20 million accretion expense mainly associated with discounted provisions.

For further information, refer to note 2, Financial income and expenses.

The year 2010

The net interest expense in 2010 was EUR 27 million lower than in 2009, mainly as a result of lower interest expense.

In 2010, income from the sale of securities of EUR 162 million was mainly attributable to the sale of NXP shares. In 2009, income from the sale of securities totaled EUR 126 million. This included a EUR 69 million gain from the sale of the remaining shares in LG Display, and a EUR 48 million gain from the sale of the remaining shares in Pace Micro Technology.

2009 was impacted by impairment charges amounting to EUR 58 million, mainly from shareholdings in NXP.

Other financial expenses amounted to a EUR 56 million expense in 2010, compared to EUR 22 million income in 2009. 2010 primarily consisted of a EUR 21 million loss related to the revaluation of the convertible bonds received from TPV Technology and CBaySystems Holdings (CBAY), and a EUR 20 million accretion expense mainly associated with discounted provisions.

Other financial expenses in 2009 primarily consisted of a EUR 20 million gain related to the revaluation of the convertible bonds received from TPV Technology and CBAY, and dividend income totaling EUR 16 million, EUR 12 million of which related to holdings in LG Display. Other financial expenses included EUR 15 million accretion expenses, mainly associated with discounted asbestos provisions.

For further information, refer to note 2, Financial income and expenses.

5.1.6 Income taxes

The year 2011

Income taxes amounted to EUR 283 million, despite losses incurred for the year, mainly due to goodwill impairment losses, which are largely non-tax-deductible. The tax charge was EUR 216 million lower than in 2010 due to lower taxable earnings, partly offset by higher incidental tax expenses.

The tax burden in 2011 corresponded to an effective income tax rate of negative 55.6%, compared to a positive 25.5% in 2010. The effective income tax rate is negative attributable to goodwill impairment losses of EUR 1,355 million, which are largely non-tax-deductible. Excluding the non-tax-deductible goodwill impairment losses, the effective income tax rate increased mainly due to a change in the mix of profits and losses in various countries, a change in the country mix of income tax rates and higher new loss carry forwards not expected to be realized.

For 2012, the effective tax rate excluding incidental non- taxable items is expected to be between 32% and 35%.

For further information, refer to note 3, Income taxes.

The year 2010

Income taxes amounted to EUR 499 million, compared to EUR 99 million in 2009. The year-on-year increase was largely attributable to higher taxable earnings.

The tax burden in 2010 corresponded to an effective tax rate of 25.5%, compared to 19.9% in 2009. The increase in the effective tax rate was attributable to a change in the country mix of income tax rates and a change in the mix of profits and losses in the various countries, as well as

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2009 s recognition of a deferred tax asset for Lumileds previously not recognized. This was partly offset by a number of tax settlements.

Reference is made to note 3, Income taxes.

5.1.7 Results of investments in associates

The year 2011

The results related to investments in associates declined from EUR 18 million in 2010 to EUR 16 million in 2011, largely attributable to the results on the sale of shares of EUR 5 million in 2010.

Results of investments in associates

in millions of euros

	2009	2010	2011
Company s participation in income	23	14	18
Results on sale of shares		5	
(Reversal of) investment impairment and other charges	54	(1)	(2)
	77	18	16

The company s participation in income increased from EUR 14 million in 2010 to EUR 18 million in 2011, mainly attributable to results on Intertrust.

For further information, refer to note 4, Investments in associates.

The year 2010

The results related to investments in associates declined from EUR 77 million in 2009 to EUR 18 million in 2010.

The company s participation in income declined from EUR 23 million in 2009 to EUR 14 million in 2010, mainly due to the sale of our remaining stake in TPV Technology.

In 2009, following recovery of the TPV share price, the accumulated value adjustment of the shareholding in TPV recognized in 2008 was reversed by EUR 55 million. The company s participation in income of EUR 23 million in 2009 was mainly attributable to results on Intertrust.

For further information, refer to note 4, Investments in associates.

5.1.8 Non-controlling interests

The year 2011

Net income attributable to non-controlling interests amounted to EUR 4 million in 2011, compared to EUR 6 million in 2010.

The year 2010

Net income attributable to non-controlling interests amounted to EUR 6 million in 2010, compared to EUR 14 million in 2009.

5.1.9 Discontinued operations

In connection with the announcement made on April 18th of the Television long-term strategic partnership with TPV Technology Limited, the results of the Television business are reported separately as discontinued operations. Consequently, the related results, including transaction gains and losses, are shown separately in the financial statements under Discontinued operations.

The loss from discontinued operations of EUR 515 million was mainly due to the transaction loss recorded in connection with the sale of our Television business of EUR 353 million (after tax), which included a provision for an onerous contract for the loss recognized

upon signing the agreement with TPV, accruals for the expected costs of disentanglement and value adjustments to assets. In addition, the net operational results of the business were an after-tax loss of EUR 162 million. The transaction is expected to close in the first quarter of 2012.

For further information, refer to note 5, Discontinued operations and other assets classified as held for sale.

5.1.10 Net income

The year 2011

Net income decreased from EUR 1,452 million in 2010 to a negative EUR 1,291 million in 2011. The decrease was largely due to EUR 2,349 million lower IFO and EUR 489 million higher costs related to discontinued operations, partly offset by EUR 216 million lower income tax charges.

Net income attributable to shareholders per common share decreased from EUR 1.54 per common share in 2010 to negative EUR 1.36 per common share in 2011.

The year 2010

Net income increased from EUR 424 million in 2009 to EUR 1,452 million. The improvement was driven by EUR 1,420 million higher IFO and EUR 41 million lower costs in Financial income and expenses, partly offset by EUR 400 million higher income tax charges and EUR 59 million lower income from our investments in associates.

Net income attributable to shareholders per common share increased from EUR 0.46 per common share in 2009 to EUR 1.54 per common share in 2010.

5.1.11 Acquisitions and divestments

In 2011, Philips completed six strategically-aligned acquisitions, benefiting all three operating sectors.

In 2011, acquisitions resulted in post-merger integration charges totaling EUR 74 million: Healthcare EUR 17 million, Consumer Lifestyle EUR 45 million, and Lighting EUR 12 million.

In 2010, acquisitions led to post-merger integration charges totaling EUR 70 million: Healthcare EUR 29 million, Consumer Lifestyle EUR 18 million, and Lighting EUR 23 million.

For further information, refer to note 7, Acquisitions and divestments.

Acquisitions

Within Healthcare, we completed three acquisitions to expand our global presence and expand our capabilities: Sectra, AllParts Medical and Dameca. In Sweden, we acquired the mammography equipment line of Sectra. We acquired Denmark-based Dameca, a global provider of anesthesia machines and accessories for the operating room. In the US, we acquired AllParts Medical, a provider of imaging equipment parts and training that expands our capabilities in imaging equipment services.

Within Consumer Lifestyle, Philips completed two acquisitions that underline the importance Philips attaches to building business creation capabilities in growth geographies. In India, we acquired the assets of the Preethi business, a leading kitchen appliances company in India. In China, we acquired Povos, a leading kitchen appliances company in China.

Within Lighting, Philips acquired Optimum Lighting, strengthening its position within energy-efficient professional lighting solutions in North America.

In 2010, we completed eleven acquisitions. Healthcare acquisitions included Somnolyzer, Tesco, Apex, CDP Medical, Wheb Sistemas and medSage Technologies. Within Lighting, Philips completed the acquisitions of Luceplan, Burton, Street Lighting Controls from Amplex A/S and NCW. Within Consumer Lifestyle, Philips acquired Discus.

In 2009, we completed eight acquisitions. Healthcare acquisitions included Meditronics, Traxtal and InnerCool. Within Lighting, Philips completed the acquisition of four companies: Dynalite, Teletrol Systems, Ilti Luce and Selecon. Within Consumer Lifestyle, Philips acquired Saeco.

Divestments

In 2011, Philips divested 80% of the shares in Assembléon. The Assembléon shares were sold to H2 Equity Partners, an Amsterdam-based private equity firm, for a consideration of EUR 14 million.

In 2010, Philips divested 9.4% of the shares in TPV Technology Ltd (TPV). The TPV shares were sold to CEIC Ltd, a Hong Kong-based technology company, for a cash consideration of EUR 98 million.

In 2009, Philips sold its shares in FIMI to Barco NV, in line with its strategy to divest non-core activities and focus on expanding its growth platforms.

For details, please refer to note 7, Acquisitions and divestments.

5.1.12 Performance by geographic cluster

The year 2011

In 2011, sales grew 4% on a comparable basis (1% nominally), driven by growth in Healthcare and Lighting, notably in growth geographies.

Comparable sales growth by geographic cluster[1)]

as a %

1) For a reconciliation to the most directly comparable GAAP measures, see chapter 15, Reconciliation of non-GAAP information, of this report

Sales in mature geographies were EUR 247 million lower than in 2010, but 1% higher on a comparable basis. Sales in Western Europe were impacted by the macroeconomic developments, resulting in lower nominal sales for all sectors, particularly in the fourth quarter. Lighting sales in Western Europe showed a slight increase on a comparable basis. Sales in North America showed a slight decline from 2010 nominally, while on a comparable basis they were slightly higher than in 2010, driven by single-digit growth at Healthcare and Lighting. Both nominal and comparable sales in other mature geographies showed strong growth. Comparable sales in other mature geographies grew by double-digits at Lighting and Consumer Lifestyle, and by mid single-digit at Healthcare.

In growth geographies, sales grew by EUR 539 million, or 11% on a comparable basis, driven by double-digit growth in all sectors, notably Healthcare (15%). In China, Healthcare and Consumer Lifestyle recorded solid double-digit nominal and comparable growth. Sales in Russia also showed double-digit growth, attributable to strong sales performance at Lighting and Healthcare.

Sales per geographic cluster

in millions of euros

1) Revised to reflect an adjusted geographic cluster allocation

The year 2010

In 2010, sales grew 5% on a comparable basis, driven by growth in all sectors, notably in growth geographies.

Sales in mature geographies were EUR 885 million higher than in 2009, or 1% higher on a comparable basis. Sales in Western Europe were in line with 2009, mainly due to lower sales at Consumer Lifestyle, which were offset by growth at Healthcare. Sales in North America were slightly higher than in 2009, attributable to low single-digit growth in Lighting and Consumer Lifestyle.

Healthcare sales in North America were on par with 2009 on a comparable basis. Sales in other mature geographies, however, grew by double-digits in all sectors.

In growth geographies, sales grew by 14%, driven by growth in all sectors, notably Lighting (more than 20%). Solid double-digit growth was visible in China, driven by Healthcare and Lighting. Sales in Russia also showed double-digit growth, attributable to strong sales performance at Consumer Lifestyle and Lighting.

5.1.13 Employment

The year 2011

The total number of Philips Group employees was 121,888 at the end of 2011, compared to 116,165 at the end of 2010. Approximately 44% were employed in the Lighting sector, due to the continued vertical integration in this business. Some 31% were employed in the Healthcare sector and approximately 15% in the Consumer Lifestyle sector.

Employees per sector 2011

in FTEs at year-end

Compared to 2010, the number of employees increased by 5,723. This figure included 4,759 additional employees from acquisitions and reduction of 479 employees via divestments. The remaining increase centered primarily on Healthcare, mainly in North America.

Approximately 53% of the Philips workforce is located in mature geographies, and about 47% in growth geographies. In 2011, the number of employees in mature geographies increased slightly as headcount reduction from organizational restructuring was more than offset by additional headcount from growing businesses within Healthcare. Growth geographies headcount increased by 5,208, mainly as a result of acquisitions in Consumer Lifestyle.

Employees per sector

in FTEs at year-end

	2009	2010	2011
Healthcare[1)]	34,525	36,253	37,955
Consumer Lifestyle	13,625	14,095	18,291
Lighting	51,653	53,888	53,168
Group Management & Services	11,586	11,929	12,474
	111,389	116,165	121,888
Discontinued operations	4,764	3,610	3,353
	116,153	119,775	125,241

1) Adjusted to reflect a change of employees reported for the past periods

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Employees per geographic cluster

in FTEs at year-end

	2009[1)]	2010[1)]	2011
Western Europe	34,174	33,557	33,515
North America	27,055	27,881	28,249
Other mature geographies	3,094	3,045	3,234
Total mature geographies	64,323	64,483	64,998
Growth geographies	47,066	51,682	56,890
	111,389	116,165	121,888
Discontinued operations	4,764	3,610	3,353
	116,153	119,775	125,241

1) Adjusted to reflect a change of employees reported in the Healthcare sector

Employment

in FTEs

	2009[1)]	2010[1)]	2011
Position at beginning of year	121,654	116,153	119,775
Consolidation changes:			
acquisitions	2,432	1,457	4,759
divestments	(276)	(307)	(479)
Comparable change	(7,657)	2,472	1,186
Position at year-end	116,153	119,775	125,241
of which:			
continued operations	111,389	116,165	121,888
discontinued operations	4,764	3,610	3,353

1) Adjusted to reflect a change of employees reported in the Healthcare sector

The year 2010

The total number of employees of the Philips Group was 119,775 at the end of 2010, compared to 116,153 at the end of 2009. Approximately 45% were employed in the Lighting sector, due to the continued relatively strong vertical integration in this business. Some 30% were employed in the Healthcare sector and approximately 12% of the workforce was employed in the Consumer Lifestyle sector.

The increase in headcount in 2010 was mainly attributable to acquisitions and an increase in temporary employees in Lighting to support higher levels of activity. The number of employees increased in all sectors.

5.2 Liquidity and capital resources

Prior years results and cash flows have been restated to reflect the effect of classifying the Television business as discontinued operations in 2011.

5.2.1 Cash flows provided by continuing operations

The year 2011

Cash flows from operating activities

Net cash flow from operating activities amounted to EUR 836 million in 2011, compared to EUR 2,121 million in 2010. The year-on-year decline was largely attributable to lower cash earnings and higher working capital outflow, mainly related to accounts payable, partly offset by lower inventories and an increase in provisions. The accounts payable outflow was mainly due to the tightening of vendor payments in the operating sectors, as well as the timing of taxes payable.

Cash flows from operating activities and net capital expenditures

in millions of euros

Condensed consolidated statements of cash flows for the years ended December 31, 2009, 2010 and 2011 are presented below:

Condensed consolidated cash flow statements[1)]

in millions of euros

	2009	2010	2011
Cash flows from operating activities:			
Net income (loss)	424	1,452	(1,291)
Adjustments to reconcile net income to net cash provided by operating activities	967	669	2,127
Net cash provided by operating activities	1,391	2,121	836
Net cash (used for) provided by investing activities	(165)	(646)	(1,364)
Cash flows before financing activities[2)]	1,226	1,475	(528)
Net cash used for financing activities	(544)	(95)	(1,787)
Cash (used for) provided by continuing operations	682	1,380	(2,315)
Net cash (used for) discontinued operations	99	(22)	(364)
Effect of changes in exchange rates on cash and cash equivalents	(15)	89	(7)
Total change in cash and cash equivalents	766	1,447	(2,686)
Cash and cash equivalents at the beginning of year	3,620	4,386	5,833
Cash and cash equivalents at the end of year	4,386	5,833	3,147

1) Please refer to section 12.7, Consolidated statements of cash flows, of this report
2) Please refer to chapter 15, Reconciliation of non-GAAP information, of this report

Cash flows from investing activities

2011 cash flows from investing activities resulted in a net outflow of EUR 1,364 million, attributable to EUR 944 million cash used for net capital expenditures and EUR 552 million used for acquisitions, mainly for Povos, Preethi and Sectra. This was partly offset by EUR 106 million proceeds from sale of financial assets and divestment, mainly TCL and Digimarc shares.

2010 cash flows from investing activities resulted in a net outflow of EUR 646 million, attributable to EUR 765 million cash used for net capital expenditures and EUR 241 million used for acquisitions, mainly for Discus, NCW and medSage Technologies. This was partly offset by EUR 385 million proceeds from divestment, including the sale of 9.4% of the shares in TPV and the redemption of the TPV and CBAY convertible bonds.

Net capital expenditures

Net capital expenditures totaled EUR 944 million, which was EUR 179 million higher than 2010. Higher investments were visible in all sectors, notably additional growth-focused investments in Healthcare.

Cash flows from acquisitions, divestments and derivatives

in millions of euros

Acquisitions

Net cash impact of acquisitions in 2011 was a total of EUR 552 million, mainly related to the acquisitions for Povos, Preethi and Sectra.

In 2010, a total of EUR 241 million cash was used for acquisitions, mainly Discus, NCW and medSage Technologies.

Divestments and derivatives

Cash proceeds of EUR 106 million were received from divestments, mainly attributable to EUR 69 million for the sale of remaining shares in TCL, as well as divestments of non-strategic businesses within Consumer Lifestyle and Healthcare. Cash flows from derivatives and securities led to a net cash inflow of EUR 26 million.

In 2010, cash proceeds of EUR 385 million were received from divestments, including EUR 98 million from the sale of 9.4% shares in TPV, EUR 165 million and EUR 74 million from the redemption of the TPV and CBAY convertible bonds respectively. The transaction related to the sale of the remaining NXP shares to Philips UK pension fund which was cash-neutral. Net cash flows used for derivatives led to a EUR 25 million net outflow.

Cash flows from financing activities

Net cash used for financing activities in 2011 was EUR 1,787 million. Philips shareholders were paid EUR 711 million in the form of a dividend of which cash dividend amounted to EUR 259 million. The net impact of changes in debt was a decrease of EUR 857 million, including the redemption of a EUR 750 million bond, a USD 350 million bond and other debts totaling EUR 1,314 million, partially offset by the drawdown of EUR 200 million committed facility and other new long-term borrowing totaling EUR 457 million. Additionally, net cash outflows for share buyback and share delivery totaled EUR 671 million.

Net cash used for financing activities in 2010 was EUR 95 million. Philips shareholders were paid EUR 650 million in the form of a dividend of which cash dividend amounted to EUR 296 million. The net impact of changes in debt was an increase of EUR 136 million, including a EUR 214 million increase from finance lease and bank loans, partially offset by repayments on short-term debts and other long-term debt amounting to EUR 78 million. Additionally, net cash inflows for share delivery totaled EUR 65 million.

The year 2010

Cash flows from operating activities

Net cash flow from operating activities amounted to EUR 2,121 million in 2010, compared to EUR 1,391 million in 2009. The year-on-year improvement was largely attributable to higher earnings across all sectors and last year s EUR 485 million final asbestos settlement payment, partly offset by higher working capital requirements.

Cash flows from investing activities

2010 cash flows from investing activities resulted in a net outflow of EUR 646 million, attributable to EUR 765 million cash used for net capital expenditures and EUR 241 million used for acquisitions, chiefly for Discus, NCW and medSage Technologies. This was partly offset by EUR 385 million proceeds from divestment, including the sale of 9.4% of the shares in TPV and the redemption of the TPV and CBAY convertible bonds.

2009 cash flows from investing activities resulted in a net outflow of EUR 165 million, due to EUR 628 million cash used for net capital expenditures, EUR 301 million used for acquisitions, and EUR 38 million outflow related to derivatives and securities, partly offset by EUR 802 million inflows received mostly from the sale of other non-current financial assets (mainly LG Display and Pace Micro Technology).

Net capital expenditures

Net capital expenditures totaled EUR 765 million, which was EUR 137 million higher than 2009. Higher investments were visible in all sectors, notably additional growth-focused investments in Lighting.

Reference is made to the information under the heading Acquisitions and divestments on pages 63 and 64 of the 2010 Annual Report, which is incorporated herein by reference.

Acquisitions

In 2010, a total of EUR 241 million cash was used for acquisitions, mainly Discus (EUR 129million), NCW (EUR 13 million) and medSage Technologies (EUR 14 million).

In 2009, a total of EUR 301 million cash was used for acquisitions, mainly Saeco (EUR 171 million), Dynalite (EUR 31 million) and Traxtal (EUR 18 million).

Divestments and derivatives

In 2010, cash proceeds of EUR 385 million were received from divestments, including EUR 98 million from the sale of 9.4% shares in TPV, EUR 165 million and EUR 74 million from the redemption of the TPV and CBAY convertible bonds respectively. The transaction related to the sale of the remaining NXP shares to Philips UK pension fund was cash-neutral. Cash flows used for derivatives led to a EUR 25 million outflow.

In 2009, cash proceeds of EUR 628 million and EUR 76 million were received from the final sale of stakes in LG Display and Pace Micro Technology respectively. Cash flows from derivatives and securities led to a net cash outflow of EUR 38 million.

Cash flows from financing activities

Net cash used for financing activities in 2010 was EUR 95 million. Philips shareholders were paid EUR 650 million in the form of a dividend of which cash dividend amounted to EUR 296 million. The net impact of changes in debt was an increase of EUR 136 million, including a EUR 214 million increase from finance lease and bank loans, partially offset by repayments on short-term debts and other long-term debt amounting to EUR 78 million. Additionally, net cash inflows for share delivery totaled EUR 65 million.

Net cash used for financing activities in 2009 was EUR 544 million. Philips shareholders were paid EUR 647 million in the form of a dividend payment. The net impact of changes in debt was an increase of EUR 61 million, including the drawdown of a EUR 251 million loan, EUR 62 million increase from finance lease and bank loans, offset by repayments on short-term debts and other long- term debt amounting to EUR 252 million. Additionally, net cash inflows for share delivery totaled EUR 29 million.

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5.2.2 Cash flows from discontinued operations

The year 2011

In 2011, EUR 364 million cash was used by discontinued operations, attributable to the operating cash flows of the Television business of EUR 270 million and cash flow to investing activities of EUR 94 million.

In 2010, EUR 22 million cash was used by discontinued operations, attributable to cash flow to investing activities of EUR 56 million of the Television business and partially offset by EUR 34 million of operating cash flows.

The year 2010

In 2010, EUR 22 million cash was used by discontinued operations, attributable to cash flow to investing activities of EUR 56 million of the Television business and partially offset by EUR 34 million of operating cash flows.

In 2009, EUR 99 million cash was provided by discontinued operations, driven by EUR 153 million of operating cash flows and partially offset by EUR 54 million of cash flows to investing activities.

5.2.3 Financing

The year 2011

Condensed consolidated balance sheets for the years 2009, 2010 and 2011 are presented below:

Condensed consolidated balance sheet information[1)]

in millions of euros

	2009	2010	2011
Intangible assets	11,523	12,233	11,012
Property, plant and equipment	3,252	3,145	3,014
Inventories	2,913	3,865	3,625
Receivables	7,188	6,296	6,839
Accounts payable and other liabilities	(9,166)	(10,180)	(10,017)
Provisions	(2,450)	(2,339)	(2,639)
Other financial assets	984	596	575
Investments in associates	281	181	203
	14,525	13,797	12,612
Cash and cash equivalents	4,386	5,833	3,147
Debt	(4,267)	(4,658)	(3,860)
Net cash (debt)	119	1,175	(713)
Non-controlling interests	(49)	(46)	(34)
Shareholders equity	(14,595)	(15,046)	(12,355)
	(14,525)	(13,917)	(13,102)

[1] Please refer to section 12.6, Consolidated balance sheets, of this report

5.2.4 Cash and cash equivalents

The year 2011

In 2011, cash and cash equivalents decreased by EUR 2,686 million to EUR 3,147 million at year-end. Cash inflow from operations amounted to EUR 836 million, a total outflow on net capital expenditure of EUR 944 million, EUR 857 million from changes in debt, EUR 671 million from treasury share transactions, EUR 552 million for acquisitions, EUR 259 million of cash dividend payout, partially offset by EUR 106 million proceeds from divestments including EUR 87 million from the sale of stakes and unfavorable currency translation effects of EUR 7 million.

In 2010, cash and cash equivalents increased by EUR 1,447 million to EUR 5,833 million at year-end. Cash inflow from operations amounted to EUR 2,121 million, a total outflow on net capital expenditure of EUR 765 million, and there was EUR 385 million proceeds from divestments including EUR 268 million from the sale of stakes. This was partly offset by an outflow of EUR 296 million related to the cash dividend payout, EUR 241 million for acquisitions and favorable currency translation effects of EUR 89 million.

Cash balance movements in 2011

in millions of euros

1) Includes the sale of shares in TCL and Digimarc, and the sale of small portion of Discuss and Raytel Imagine Network
2) Please refer to chapter 15, Reconciliation of non-GAAP information, of this report
3) Includes cash inflow for derivatives, partly offset by unfavourable currency effect
4) Includes the acquisitions of Povos, Preethi and Sectra

The year 2010

In 2010, cash and cash equivalents increased by EUR 1,447 million to EUR 5,833 million at year-end. Cash inflow from operations amounted to EUR 2,121 million, a total outflow on net capital expenditure of EUR 765 million, and there was EUR 385 million proceeds from divestments including EUR 268 million from the sale of stakes. This was partly offset by an outflow of EUR 296 million related to the cash dividend payout, EUR 241 million for acquisitions and favorable currency translation effects of EUR 89 million.

In 2009, cash and cash equivalents increased by EUR 766 million to EUR 4,386 million at year-end. Cash inflow from operations amounted to EUR 1,391 million, and there was EUR 802 million proceeds from divestments including EUR 718 million from the sale of stakes. This was partly offset by an outflow of EUR 647 million related to the annual dividend, EUR 301 million for acquisitions and small unfavorable currency translation effects of EUR 15 million.

5.2.5 Debt position

The year 2011

Total debt outstanding at the end of 2011 was EUR 3,860 million, compared with EUR 4,658 million at the end of 2010.

Changes in debt

in millions of euros

	2009	2010	2011
New borrowings	(312)	(214)	(457)
Repayments	251	78	1,314
Consolidation and currency effects	(18)	(255)	(59)
Total changes in debt	(79)	(391)	798

In 2011, total debt decreased by EUR 798 million. The repayment of EUR 1,314 million included redemptions of a EUR 750 million bond, a USD 350 million bond, and EUR 217 million repayment in short-term debt. New borrowing and finance leases amounted to EUR 457 million. Other changes resulting from consolidation and currency effects led to an increase of EUR 59 million.

In 2010, total debt increased by EUR 391 million. The increase in borrowings including finance leases was EUR 214 million. Repayments under finance leases amounted to EUR 50 million, while EUR 28 million was used to reduce other long-term debt. Other changes resulting from consolidation and currency effects led to an increase of EUR 255 million.

Long-term debt as a proportion of the total debt stood at 85% at the end of 2011 with an average remaining term of 10.4 years, compared to 60% at the end of 2010.

For further information, please refer to note 19, Long-term debt and short-term debt

The year 2010

Total debt outstanding at the end of 2010 was EUR 4,658 million, compared with EUR 4,267 million at the end of 2009.

In 2010, total debt increased by EUR 391 million. The increase in borrowings including finance leases was EUR 214 million. Repayments under finance leases amounted to EUR 50 million, while EUR 28 million was used to reduce other long-term debt. Other changes resulting from consolidation and currency effects led to an increase of EUR 255 million.

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In 2009, total debt increased by EUR 79 million. In January, Philips drew upon a EUR 250 million bank loan. The increase in other borrowings including finance leases was EUR 62 million. Repayments under finance leases amounted to EUR 42 million, while EUR 6 million was used to reduce other long-term debt. Furthermore Philips repaid short-term debt of EUR 204 million. Other changes resulting from consolidation and currency effects led to an increase of EUR 18 million.

Long-term debt as a proportion of the total debt stood at 60% at the end of 2010 with an average remaining term of 10.8 years, compared to 85% at the end of 2009.

5.2.6 Net debt to group equity

The year 2011

Philips ended 2011 in a net debt position (cash and cash equivalents, net of debt) of EUR 713 million, compared to a net cash position of EUR 1,175 million at the end of 2010.

Net debt (cash) to group equity[1)]

in billions of euros

ratio: -31:131 4:96 -1:101 -8:108 5:95

1) For a reconciliation to the most directly comparable GAAP measures, see chapter 15, Reconciliation of non-GAAP information, of this report

2) Shareholders equity and non-controlling interests

The year 2010

Philips ended 2010 in a net cash position (cash and cash equivalents, net of debt) of EUR 1,175 million, compared to a net cash position of EUR 119 million at the end of 2009.

5.2.7 Shareholders equity

The year 2011

Shareholders equity decreased by EUR 2,691 million in 2011 to EUR 12,355 million at December 31, 2011. The decrease was mainly as a result of a EUR 1,291 million lower net income and EUR 447 million actuarial losses related to pension plans, as well as EUR 751 million related to the purchase of treasury shares. The dividend payment to shareholders in 2011 reduced equity by EUR 263 million. The decrease was partially offset by a EUR 86 million increase related to delivery of treasury shares and net share-based compensation plans.

Shareholders equity increased by EUR 451 million in 2010 to EUR 15,046 million at December 31, 2010. The increase was mainly as a result of a EUR 630 million improvement within total comprehensive income. The dividend payment to shareholders in 2010 reduced equity by EUR 304 million. The decrease was partially offset by a EUR 111 million increase related to delivery of treasury shares and net share-based compensation plans.

The number of outstanding common shares of Royal Philips Electronics at December 31, 2011 was 926 million (2010: 947 million).

At the end of 2011, the Company held 33.6 million shares in treasury to cover the future delivery of shares (2010: 37.7 million shares). This was in connection with the 47.1 million rights outstanding at the end of 2011 (2010: 54.9 million rights) under the Company s long-term incentive plan and convertible personnel debentures. At the end of 2011, the Company held 49.3 million shares for cancellation (2010: 1.9 million shares).

The year 2010

Shareholders equity increased by EUR 451 million in 2010 to EUR 15,046 million at December 31, 2010. The increase was mainly as a result of a EUR 630 million improvement within total comprehensive income. The dividend payment to shareholders in 2010 reduced equity by EUR 304 million. The decrease was partially offset by a EUR 111 million increase related to delivery of treasury shares and net share-based compensation plans.

Shareholders equity declined by EUR 949 million in 2009 to EUR 14,595 million at December 31, 2009. The decrease was mainly as a result of a EUR 404 million reduction from total comprehensive income. The dividend payment to shareholders in 2009 further reduced equity by EUR 647 million. The decrease was partially offset by a EUR 101 million increase related to re-issuance of treasury shares and net share-based compensation plans.

The number of outstanding common shares of Royal Philips Electronics at December 31, 2010 was 947 million (2009: 927 million).

At the end of 2010, the Company held 37.7 million shares in treasury to cover the future delivery of shares (2009: 43.1 million shares). This was in connection with the 54.9 million rights outstanding at the end of 2010 (2009: 62.1

million rights) under the Company s long-term incentive plan and convertible personnel debentures. At the end of 2010, the Company held 1.9 million shares for cancellation (2009: 1.9 million shares).

5.2.8 Liquidity position

Including the Company s net debt (cash) position (cash and cash equivalents, net of debt), listed available-for-sale financial assets, as well as its EUR 1.8 billion revolving credit facility, a EUR 900 million bilateral credit facility and a EUR 500 million bilateral credit facility, the Company had access to net available liquid resources of EUR 2,597 million as of December 31, 2011, compared to EUR 3,445 million one year earlier.

Liquidity position

in millions of euros

	2009	2010	2011
Cash and cash equivalents	4,386	5,833	3,147
Committed revolving credit facility/ CP program/Bilateral loan	1,936	2,000	3,200
Liquidity	6,322	7,833	6,347
Available-for-sale financial assets at market value	244	270	110
Main listed investments in associates at market value	113		
Short-term debt	(627)	(1,840)	(582)
Long-term debt	(3,640)	(2,818)	(3,278)
Net available liquidity resources	2,412	3,445	2,597

The fair value of the Company s available-for-sale financial assets, based on quoted market prices at December 31, 2011, amounted to EUR 110 million. Philips disposed of its remaining shareholdings in TCL and Digimarc in 2011.

Philips has a EUR 1.8 billion committed revolving credit facility due in 2015 that can be used for general corporate purposes. In addition, Philips also has a EUR 900 million committed bilateral credit facility in place that can be drawn before July 2013. Furthermore Philips has a USD 2.5 billion commercial paper program, under which it can issue commercial paper up to 364 days in tenor, both in the US and in Europe, in any major freely convertible currency. There is a panel of banks, in Europe and in the US, which service the program. The interest is at market rates prevailing at the time of issuance of the commercial paper. There is no collateral requirement in the commercial paper program. Also, there are no limitations on Philips use of the program. As at December 31, 2011, Philips did not have any loans outstanding under these facilities.

Philips existing long-term debt is rated A3 (with negative outlook as of February 8, 2012) by Moody s and A- (with negative outlook as of February 3, 2012) by Standard & Poor s. It is Philips objective to manage our financial ratios to be in line with an A rating. There is no assurance that we will be able to achieve this goal. Ratings are subject to change at any time. Outstanding long-term bonds and credit facilities do not have a material adverse change clause, financial covenants or credit-rating-related acceleration possibilities.

As at December 31, 2011, Philips had total cash and cash equivalents of EUR 3,147 million. Philips pools cash from subsidiaries to the extent legally and economically feasible. Cash not pooled remains available for local operational or investment needs. Philips had a total gross debt position of EUR 3,860 million at year-end 2011.

We believe our current working capital is sufficient to meet our present working capital requirements.

5.2.9 Cash obligations

Contractual cash obligations

Presented below is a summary of the Group s contractual cash obligations and commitments at December 31, 2011.

Contractual cash obligations at December 31, 2011

in millions of euros[1)]

		payments due by period			
	total	**less than 1 year**	**1-3 years**	**3-5 years**	**after 5 years**
Long term debt	3,213	80	923	1	2,209
Finance lease obligations	218	60	90	33	35
Short-term debt	443	443			
Operating leases	1,017	242	371	224	180
Derivative liabilities	749	208	474	67	
Interest on debt[2)]	1,737	138	268	215	1,116
Purchase obligations[3)]	505	242	211	29	23
Trade and other payables	3,346	3,346			
	11,228	4,759	2,337	569	3,563

1) Data in this table is undiscounted

2) Approximately 27% of the debt bears interest at a floating rate. Majority of the interest payments on variable interest rate loans in the table above reflect market forward interest rates at the period end and these amounts may change as market interest rate changes

3) Philips has commitments related to the ordinary course of business which in general relate to contracts and purchase order commitments for less than 12 months. In the table, only the commitments for multiple years are presented, including their short-term portion

Philips has no material commitments for capital expenditures.

On December 1, 2009, Philips entered into an outsourcing agreement to acquire IT services from T-Systems GmbH over a period of 5 years at a total cost of approximately EUR 300 million. The agreement, which is effective January 1, 2010, provides that penalties may be charged to the Company if Philips terminates the agreement prior to its expiration. The termination penalties range from EUR 40 million if the agreement is cancelled within 12 months to EUR 6 million if the agreement is cancelled within 36 months.

Additionally, Philips has a number of commercial agreements, such as supply agreements, which provide that certain penalties may be charged to the Company if it does not fulfill its commitments.

Certain Philips suppliers factor their trade receivables from Philips with third parties through supplier finance arrangements. At December 31, 2011 approximately EUR 283 million of the Philips accounts payables were known to have been sold onward under such arrangements whereby Philips confirms invoices. Philips continues to recognize these liabilities as trade payables and will settle the liabilities in line with the original payment terms of the related invoices.

As part of the recovery plan for the UK pension fund, Philips Electronics UK has committed to a contingent cash contribution scheme as a back-up for liability savings to the UK fund to be realized through a member choice program. If this member choice program fails to deliver part or all of the expected liability savings with a net present value of GBP 250 million, Philips Electronics UK will pay cash contributions into the UK pension fund to make up for the difference during the years 2015 and 2022. No (further) cash payments will be made under the scheme when the UK pension fund is fully funded.

Other cash commitments

The Company and its subsidiaries sponsor pension plans in many countries in accordance with legal requirements, customs and the local situation in the countries involved. Additionally, certain postretirement benefits are provided in certain countries. The Company is reviewing the future funding of the existing regulatory deficits in pension plans in the US and UK. Refer to note 29, Pensions and other postretirement benefits for a discussion of the plans and expected cash outflows.

The company had EUR 169 million restructuring-related provisions by the end of 2011, of which EUR 118 million is expected to result in cash outflows in 2012. Refer to note 20, Provisions for details of restructuring provisions and potential cash flow impact for 2011 and further.

A proposal will be submitted to the General Meeting of Shareholders to pay a dividend of EUR 0.75 per common share (up to EUR 695 million), in cash or shares at the option of the shareholder, against the retained earnings of the Company.

Guarantees

Philips   policy is to provide guarantees and other letters of support only in writing. Philips does not provide other forms of support. At the end of 2011, the total fair value of guarantees recognized by Philips in other non-current liabilities was EUR 9 million. The following table outlines the total outstanding off-balance sheet credit-related guarantees and business-related guarantees provided by Philips for the benefit of unconsolidated companies and third parties as at December 31, 2010 and 2011.

Expiration per period 2011

in millions of euros

	total amounts committed	less than 1 year	1-5 years	after 5 years
Business-related guarantees	297	99	126	72

Credit-related guarantees	39	22		17
	336	121	126	89

Expiration per period 2010

in millions of euros

	total amounts committed	less than 1 year	1-5 years	after 5 years
Business-related guarantees	302	100	133	69
Credit-related guarantees	49	22	8	19
	351	122	141	88

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5.3 Other performance measures

Prior years results and cash flows have been restated to reflect the effect of classifying the Television business as discontinued operations in 2011.

The section Other performance measures provides an insight into the performance of key cross-sector functions brand, marketing, research and development and supply management in 2011.

5.3.1 Marketing

The year 2011

Brand and Customer Experience

In 2011, Philips continued to focus on building brand loyalty amongst its professional and consumer audiences, a key element of its brand strategy. The deployment of this strategy led to a rise from 42nd to 41st position among the world s 100 most valuable brands, as measured by Interbrand. Additionally, Philips maintained its estimated brand value at USD 8.7 billion, despite the challenging economic environment throughout 2011, particularly in Europe.

Philips total 2011 marketing expenses approximated EUR 938 million, an increase of 12% compared to 2010. Consistent with 2010, the company allocated a higher proportion of its total marketing spend towards growth geographies and strategic markets, priority areas for the company s growth strategy. Accordingly, the company increased its marketing spend in growth geographies by 15% compared to 2010. Philips also continued to align its businesses around customers and markets, maintaining its level of local marketing investment as a percentage of sales at approximately 5% in growth geographies in both 2010 and 2011. Total 2011 marketing investment as a % of sales approximated 4.2%, compared to 3.7% in 2010.

In 2011, we continued to expand our coverage of the Net Promoter Score (NPS) program to include additional markets strategic to Philips growth. With regard to NPS performance in 2011, the company achieved its leadership targets at Lighting, and strengthened its outright leadership position at Consumer Lifestyle. Philips maintains its strong leadership positions in a large number of its key geographies. In China, it attained new leadership positions in Lighting, whilst retaining all existing Healthcare leadership positions. It also showed an improvement in performance at Healthcare and Consumer Lifestyle in the US, our largest healthcare market. In Europe, Philips showed a mixed performance, with gains in LED lighting in Germany, and a decline at Healthcare in France. Looking ahead to 2012 and beyond, the company will continue to use NPS as a measure of customer experience. In line with its Accelerate! transformation aimed at winning customers in its markets and the pursuit of excellence in the marketplace, it will focus on outright NPS leadership relative to competition, as well as its own absolute position with customers.

Marketing expenses

in millions of euros

The year 2010

Philips total 2010 marketing expenses approximated EUR 835 million, a 17% increase compared to 2009. The additional spend was primarily to support the company s marketing strategy of more focused growth in growth and other strategic geographies. In line with this, the company increased its 2010 marketing spend in key growth geographies by 33% compared to 2009. Total 2010 marketing investment in growth geographies approximated 4.0% of sales, compared to 3.6% of sales in 2009.

5.3.2 Research & development

The year 2011

R&D spending increased as a percentage of sales from 6.7% in 2010 to 7.1%. Philips has continued to expand its vast knowledge and intellectual property base. Early and continuous involvement of customers in new technologies, application and business concepts ensures deep insight into their needs the foundation for our innovations. Innovation leading to new businesses in incubators and internal ventures and Emerging Business Areas is managed separately from the traditional business to ensure focus on these growth initiatives. The effectiveness of innovation has been improved by streamlining our organization in Corporate Technologies, leading to more focus, alignment and enhanced offering of value propositions. The scope of the new organization covers front end innovation, i.e. early innovation and pre-development activities, supplemented by small series production. Within the Accelerate! program this approach started to show results in terms of increased speed to market.

Healthcare R&D spend has increased substantially by EUR 42 million, to drive co-leadership in Imaging Systems and leadership in Patient Care and Clinical Informatics. Also, in Consumer Lifestyle we increased the R&D spend by EUR 31 million, to drive category leadership in Male Grooming, Oral Healthcare, Kitchen Appliances and Coffee. In Lighting, we increased our R&D investment by 15% or EUR 54 million compared to 2010, to accelerate transformation to LED, applications and solutions, to maintain our leadership position in LED lighting innovation (e.g. L-prize), and to ensure maintenance of our lead over competition, including our leading IP position. In GM&S, R&D expenses were reduced by EUR 10 million, creating more focus.

Research and development expenses per sector

in millions of euros

	2009	2010	2011
Healthcare	679	698	740
Consumer Lifestyle	300	282	313
Lighting	351	355	409
Group Management & Services	212	158	148
Philips Group	1,542	1,493	1,610

The year 2010

In 2010, Philips investment in R&D activities amounted to EUR 1,493 million (6.7% of sales), compared with EUR 1,542 million (7.7% of sales) in 2009.

5.3.3 Supply management

The Supply organization encompasses four functions: Commercial Supply Chain, Customer Service, Operations and Purchasing. Collectively, they represent around 61,000 Philips employees and are responsible for sourcing, manufacturing and delivering products and solutions.

Management of shortages and management of commodity price increases

The recovery of the global economy led to tight supply of semiconductor components, in particular, in the course of 2011. The scarcity of and increased prices for commodities like copper and phosphor led to upward price pressure. We were largely able to negotiate price decreases, delay price increases and reduce volatility through commodity hedging with our suppliers. Raw material price trends in the last quarter of the year started to move in the opposite direction; prices are trending down again in anticipation of a possible second period of economic turbulence with generally lower demand ahead. Supply achieved 4.9% savings on the Bill of Material (BOM) and 5.2% savings on Non Product Related (NPR) purchasing. Forecast reliability and sales/operational planning processes have improved, for both the short and longer term, resulting in reduced risk. Increased efforts on local talent hiring and breeding in growth geographies are being made to secure the inflow of professionals into supply functions for the future.

Concentration and consolidation of supply base

Philips Supply continued its focus on leveraging the base of selected suppliers. In both BOM and NPR the number of suppliers continued to be reduced. Creating long-term strategic partnerships with suppliers is an important enabler of Philips growth ambitions. Further alignment and standardization of payment terms continued to positively influence Days Payable Outstanding (DPO).

Supplier risk management and business interruption

Our strategic buyers are constantly monitoring their supplier portfolio; risk parameters are measured and contingency plans are in place. Extreme circumstances impacted supply performance in 2011; the earthquake and tsunami in Japan in March 2011 exposed vulnerability in our complex global supply network. During the Japan crisis the complexity of the suppliers and indirect market effects such as hoarding were discovered. Dedicated teams worked both locally in Japan and internationally with suppliers and their suppliers to mitigate risks. Similarly, these experiences have been applied to help deal with the impact of the flooding in Thailand, where supply of a critical component was interrupted, resulting in a significant supply continuity risk, which was handled successfully.

Sustainability in the supply chain

Philips remains focused on improving working conditions and environmental performance in its supply chain and expects suppliers to share this ambition. We support suppliers in this journey and engage with governmental and civil society organizations and other business partners to further embed sustainability in the supply chain. For more information, refer to Supplier performance section (in the chapter Sustainability Statements).

New venture integration

Purchasing participates in the Philips New Venture Integration team. The focus is on creating value via spend savings and cash improvements and on risk mitigation related to sustainability and financial weakness of the supply chain of the newly acquired company.

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5.4 Sustainability

Strategic priorities

Our businesses provide innovative solutions that address the major trends affecting the world the demand for affordable healthcare, the need for greater energy efficiency and the desire for personal well-being. At Philips, sustainability is all about enhancing the health and well-being of individuals and the communities they live in. At the same time we constantly endeavor to improve the environmental performance of our products and processes, and to drive sustainability throughout the supply chain.

Notwithstanding the challenging economic environment, Philips has kept its focus on sustainability in 2011. This is rooted in our long-standing belief that sustainability is a key enabler for growth and offers opportunities to innovate our way out of the economic crisis. Therefore, sustainability is an integral part of Philips strategy and Deliver on our EcoVision sustainability commitments was one of the topics on the 2011 Management Agenda.

By focusing on three sustainability leadership key performance indicators in which we can bring our competencies to bear, namely care , energy efficiency and materials we aim to deliver on our 2015 commitments:

Bringing care to people

- Target: 500 million lives touched by 2015

Improving the energy efficiency of Philips products

- Target: 50% improvement by 2015 (for the average total product portfolio) compared to 2009

Closing the materials loop

- Target: Double global collection and recycling and the amount of recycled materials in products by 2015 compared to 2009

In 2011, we already touched over 465 million lives, mainly driven by our Healthcare sector. Further, the energy efficiency of the products we sold improved slightly (some 2% in 2011 and 8% compared to 2009). Our Lighting sector contributed most to this indicator and notwithstanding strong LED sales, the energy efficiency improvement in the total product portfolio sold in 2011 was limited as traditional lamps were still much in demand. With regard to Closing the materials loop , our global collection and recycling totaled to about 35,000 tons and the amount of recycled materials in our products increased to around 10,000 tons. More importantly, roadmaps have been developed to double the amount of recycled materials in our products with a focus on recycled plastics. More information on these parameters can be found in chapter 14, Sustainability statements, of this report.

External recognition

In 2011, we gained external recognition on various occasions. We obtained the highest status in the Dow Jones Sustainability Index (super-sector leader) and we achieved the highest scores in the Carbon Disclosure Project, both for our Carbon Disclosure and for our Carbon Performance.

5.4.1 EcoVision

Philips has a long sustainability history; our founding fathers embedded sustainability at the heart of the company from its earliest days. In 1998, we launched our first EcoVision program and set sustainability targets focused on our own operations and products. We also started to focus on sustainability in our supply chain in 2003. Later programs included enhanced Manufacturing, Green Innovation and Carbon Footprint targets thereby extending our sustainability scope.

In 2010 we expressed our ambition to be a leader in sustainability by focusing not only on the environmental impact of our products and operations, but also on strengthening social dimension and defined ambitious targets for 2015 along both axes, paving the way for sustainable innovation as visualized below.

The challenge on the ecological axis is to optimize our impact on the environment, especially on climate change and resource scarcity. On the social axis, we aim to increase our contribution to the health and well-being of people. Combined, this will help the transition towards a sustainable society in which ultimately 9 billion people can live a healthy and fulfilling life within the carrying capacity of one planet.

Green Product sales

In 2011, sales from Green Products increased to EUR 8,805 million, contributing significantly to the total revenue stream. As a percentage of the Group total, Green Product sales rose to 39%, up from 36% in 2010, and on track to reach the new target of 50% in 2015.

All sectors contributed to the overall sales increase, but the increase at Healthcare was the most significant, followed by Lighting.

Most of the environmental improvements were realized in energy efficiency of products, one of the Green Focal Areas in our EcoDesign process and an important objective of our EcoVision program. There was also growing attention for substances of concern and recycling in all sectors.

Green Product sales by sector

in millions of euros

Green Innovation

Green Innovation is the Research & Development spend related to the development of new generations of Green Products and Green Technologies. Having achieved the target of a EUR 1 billion cumulative investment in 2010, two years ahead of schedule, we then announced plans to invest a cumulative EUR 2 billion during the coming 5 years. Philips invested some EUR 470 million in Green Innovation in 2011, with a very strong contribution from Lighting in particular.

Healthcare s innovation projects are targeted at making a difference wherever care is provided in the hospital, the home and points in-between which has brought us closer to our goal of touching 500 million lives annually around the globe. The sector focuses on reducing energy consumption, weight, lifecycle management, hazardous substances and radiation dosage.

Green Innovation at Consumer Lifestyle amounted to EUR 67 million and the sector continued its work on improving the energy efficiency of the products, the closing of the materials loop and the voluntarily phase-out of polyvinyl chloride (PVC) and brominated flame retardants (BFR), enabling our Personal Care businesses to launch products which are completely free of these substances. Other results of Consumer Lifestyle s Green Innovation activities are the EcoCare Iron and the Senseo Viva Café Eco.

The Lighting sector accounts for over 60% of the total spend on Green Innovation and also contributes to over 50% of Philips Green Product sales. The focus is on developing new energy-efficient lighting solutions, further enhancing current Green Products and driving toward technological breakthroughs, such as solid-state lighting and water purification through UV light.

Corporate Technologies invested more than EUR 36 million on a Green Innovation activity portfolio mainly focused on energy efficiency, care and the reduction of waste and water consumption. Philips Research developed an EcoVision portfolio mapping tool in which innovation projects are mapped along the environmental and social dimension. The tool will be made available to the innovation community within Philips to further drive sustainable innovation.

Green Innovation investment

in millions of euros

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Operational carbon footprint and energy efficiency

In 2011, we took another step towards reaching our target of 25% CO_2 reduction by 2012, as operational CO_2 emissions decreased 4%. CO_2 emissions from manufacturing decreased 8% due to a number of reasons, including our ongoing energy efficiency program, the changing industrial footprint and the increase in purchased electricity from renewable sources. CO_2 emissions from non-industrial sites decreased 2%, partly because of our continued focus on the most efficient use of facility space, for instance with our Work Place Innovation program (which enables flex-working), but also due to the increased share of purchased electricity from renewable sources.

As a result of our green lease car policy, our lease car fleet continues to become more CO_2 efficient. Consequently, the average CO_2 per kilometer further decreased 8% compared to last year. Total emissions from business travel increased, however, due to a higher number of airplane travel movements. We continue to promote video conferencing as an alternative to travel. CO_2 emissions from logistics decreased 2%, because of our continued focus on efficient container utilization, reducing mileage in road freight, and the shift from air to sea freight, which is cleaner and more cost effective.

Our operational energy efficiency improved 4%, from 1.29 terajoules per million euro sales in 2010 to 1.24 terajoules per million euro sales in 2011.

Carbon emissions in our Supply Chain

In 2011, we also performed a study to quantify the CO_2 emissions of our total supply chain which allows us to target our carbon reduction actions. Total emissions in the supply chain were estimated at 5.6 million tons.

Operational energy efficiency

in terajoules per million euro sales

5.4.2 Green Manufacturing 2015

We developed our Green Manufacturing 2015 program in 2010 as we wanted to continue our efforts to improve our environmental performance in manufacturing. The program focuses on most contributors to climate change, recycling of waste, reduction of water consumption and reduction of restricted and hazardous substances.

Full details, including our 2015 targets, can be found in chapter 14, Sustainability statements, of this report.

5.4.3 Social performance

Employee engagement

In 2011, 87% of our employees took part in the Engagement Survey. The Employee Engagement Index the single measure of the overall level of employee engagement at Philips reached 76%, marking a 1 point decrease. The target for 2011 was to maintain the EEI at the external high-performance benchmark level of 77%.

Equally important is the insight we gained into ways in which we can improve. For 2012, the focus will be put on improving the engagement level within customer facing functions and in the area of confidence and trust.

Diversity and inclusion

In 2011, Philips made progress towards its targets relating to the diversity of the company s executive population. The share of female executives increased to 13% compared to 11% in 2010 two percentage points off the 2012 target of 15% female executives. While the Healthcare and Consumer Lifestyle sector traditionally had a better representation of women at senior and executive grades, 2011 saw Philips successfully start to tackle the concern on low numbers of female executives in the Lighting sector. Their share approximately doubled to 14% in 2011.

Female Executives

as a % of total

Of a total of 68 newly appointed executives, resulting from internal promotions, 17% were women. Almost 30% of newly hired executives were female, demonstrating our commitment to increasing gender diversity in the company s leadership beyond the internally available pipeline. With Carole Wainaina, who joined Philips in 2011 as the new Chief HR Officer, Philips once more has a woman on its Executive Committee.

In 2011, Philips also achieved an increase of the share of women especially in senior professional and management roles, clear proof points of the companies ambition to drive gender diversity more broadly and ensure a sustainable internal pipeline of highly qualified women from junior level upwards.

In line with the growing importance of BRIC countries as part of the Philips business, the share of executives with Brazilian, Russian, Indian and Chinese nationality increased from 5% in 2010 to over 8% in 2011. The 2012 target is 10% of the total executive population. In 2011, Patrick Kung, Market Leader Greater China, was appointed to the Executive Committee. Overall, the 567 executives of Philips represent 31 different nationalities.

Developing our people

Our learning strategy focuses on building skills that are strongly aligned with business needs. In 2011, we continued to streamline our classroom offerings in close alignment with businesses and functions to focus on their key priorities. The second important driver of our learning strategy is providing employees with free and unlimited access to a wide range of online learning options to drive their personal development and growth.

Participation in these priority programs and free unlimited online courses increased significantly, with over 39,000 enrollments compared with 20,000 in 2010. Functional Core Curricula enrollment was over 25,000 in 2011, an increase from 15,500 in 2010. These Core Curricula have been developed for functions such as Marketing, Sales, Customer Services, IT, HRM, Supply Management and Finance. Moreover, we had over 30,000 employees participating in various ethics and compliance related training sessions.

Our flagship leadership development programs for our talent pool are run in collaboration with leading business schools with a strong emphasis on blended learning. In 2011, our Inspire program facilitated the completion of 18 project assignments by 147 high potentials. Top potentials in the Octagon program completed 8 business projects. These business projects are sponsored by senior business leaders and focus on Healthcare and Well-being, targeting growth geographies, the US and South Africa.

Our leadership development programs will be extended and upgraded to reflect business needs and the need for local customization, building on the Accelerate! leadership behaviors and culture change.

In line with our Grow with Philips program, 76% of newly appointed executives were promotions and 24% external hires.

Health and safety

We regret to report two fatalities in 2011, of which one was related to a safety accident and one to a traffic accident whilst commuting.

In 2011, we recorded 405 Lost Workday Injuries cases, i.e. injury cases where the injured person is unable to work the day after the injury. This was a 16% decrease compared with 2010. The rate of Lost Workday Injuries also decreased to 0.38 per 100 FTEs, compared to 0.50 in 2010.

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The decrease in Lost Workday Injuries was visible in all sectors, but strongest in Lighting that started to see the results of its Safety First health and safety program. We also updated our Health & Safety (H&S) policy and deployed a H&S manual to all sites to help them structurally improve the H&S culture.

Lost Workday Injuries

per 100 FTEs

5.4.4 General Business Principles

The Philips General Business Principles (GBP) govern Philips business decisions and actions throughout the world, applying equally to corporate actions and the behavior of individual employees. They incorporate the fundamental principles within Philips for doing business.

The GBP are available in most of the local languages and are an integral part of the labor contracts in virtually all countries where Philips has business activities. Responsibility for compliance with the principles rests primarily with the management of each business. Every country organization and each main production site has a compliance officer. Confirmation of compliance with the GBP is an integral part of the annual Statement on Business Controls that has to be issued by the management of each business unit. The GBP incorporate a whistleblower policy, standardized complaint reporting and a formal escalation procedure.

The global implementation of the One Philips Ethics hotline seeks to ensure that alleged violations are registered and dealt with consistently within one company-wide system.

To drive the practical deployment of the GBP, a set of directives has been published, which are applicable to all employees. There are also separate directives which apply to specific categories of employees, e.g. the Supply Management Code of Ethics and Financial Code of Ethics. Details can be found at www.philips.com/gbp.

Ongoing training

The global roll-out of the updated version of the mandatory web-based GBP training, which is designed to reinforce awareness of the need for compliance with the GBP, was completed in 23 languages.

More information on the Philips GBP can be found in chapter 7, Risk management, of this report. Results of the monitoring in place are provided in the chapter 14, Sustainability statements, of this report.

5.4.5 Supplier performance

Increasingly, our products are being created and manufactured in close cooperation with a wide range of business partners, both in the electronics industry and other industries. Philips is committed to being a leader in sustainability. Clearly, we need our business partners to share our commitment, not just in the development and manufacturing of products but also in the way they conduct their business. Our Supplier Sustainability Involvement Program is designed to engage our suppliers on a shared journey towards leadership in sustainability.

Our suppliers

As a leading company in sustainability, Philips will act as a catalyst towards our suppliers and support our suppliers in their pursuit of continuous improvement of social and environmental performance. We recognize that this is a huge challenge requiring industry-wide effort in collaboration with other societal stakeholders. Therefore, we remain active in the Electronic Industry Citizenship Coalition (EICC) and encourage our strategic suppliers to join the EICC too. We will invite our strategic suppliers to jointly explore the opportunities to accelerate our product innovation towards our EcoVision objectives. We will also continue to seek active cooperation with other societal stakeholders, either directly or through institutions like the EICC, the multi-stakeholder program from the

Sustainable Trade Initiative and the OECD.

Supplier Sustainability Involvement Program

The Philips Supplier Sustainability Involvement Program is our overarching program to help improve the sustainability performance of our suppliers. We create commitment from our suppliers by requiring them to comply with our Philips Supplier Sustainability Declaration and the Regulated Substances List. The Philips Supplier Sustainability Declaration is based on the EICC code of conduct and also includes additional requirements on Freedom of Association and Collective Bargaining. The topics covered include labor and human rights, worker health and safety, environmental impact, ethics and management systems. The Declaration is signed by suppliers as part of their purchasing contracts.

Philips uses a risk assessment to select suppliers in risk countries for inclusion in the audit program. During the audits, compliance to all sections of the Declaration is reviewed and in case of non-compliance the implementation of corrective actions is monitored.

In addition to the audit program, we developed specific projects and stakeholder engagement activities to help improve the sustainability performance of our suppliers, such as on improving on their worker-management dialogue, carbon footprinting, and compliance with the Conflict minerals provisions. For more details, see section 14.6, Supplier indicators, of this report.

2011 supplier audits

Philips conducted 212 full scope audits in 2011, including 9 joint audits conducted on behalf of Philips and other EICC member companies. During these audits an external company visited the supplier s site in risk countries for a 2 to 12 man-days audit during which compliance with all sections of the Supplier Sustainability Declaration was assessed. As in previous years the majority of the audits were done in China, representing a major part of our supply base. The total number of full scope audits conducted since we started the program in 2005 now exceeds 1,800. This number includes repeated audits, since we execute a full scope audit at our risk suppliers every 3 years.

The most frequently observed areas of non-compliance were:

- Working hours, wages and benefits: excessive overtime, continual seven-day work weeks, record-keeping of standard and overtime working hours, no payment of overtime premiums

- Emergency preparedness: inadequate fire detection and suppression systems, blocked or insufficient emergency exits

- Occupational safety: worker exposure to safety hazards, e.g. electrical shocks

- Lack of adequate management systems to safeguard compliance to the EICC code for labor and ethics, health and safety, and environment

Accumulative number of initial and continual conformance audits

Distribution of supplier audits by country

To track improvements, Philips measures the compliance rate for the identified risk suppliers, being the percentage of risk suppliers that was recently audited and has resolved all major non compliances. During 2011 we achieved a compliance rate of 72%. For more details on audit results, please refer to section 14.6, Supplier indicators, of this report.

Conflict minerals: issues further down the chain

Conflict minerals can come from many souces around the world including mines in the Democratic Republic of the Congo (DRC). Philips is concerned about the situation in the east of the DRC where proceeds from the extractives sector are used to finance rebel conflicts in the region. Philips is committed to address this issue through the means and influencing mechanisms available to us, even though Philips does not directly source minerals from the DRC and mines are typically seven or more tiers removed from our direct suppliers. During 2011 we worked with 100 priority suppliers to raise awareness and start supply chain investigations to determine the origin of the metals in our products, resulting in the identification of over 100 smelters in our supply chain that process these metals. For more details, please refer to section 14.6, Supplier indicators, of this report.

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5.5 Proposed distribution to shareholders

Pursuant to article 34 of the articles of association of Royal Philips Electronics, a dividend will first be declared on preference shares out of net income. The remainder of the net income, after reservations made with the approval of the Supervisory Board, shall be available for distribution to holders of common shares subject to shareholder approval after year-end. As of December 31, 2011, the issued share capital consists only of common shares; no preference shares have been issued. Article 33 of the articles of association of Royal Philips Electronics gives the Board of Management the power to determine what portion of the net income shall be retained by way of reserve, subject to the approval of the Supervisory Board.

A proposal will be submitted to the 2012 Annual General Meeting of Shareholders to declare a dividend of EUR 0.75 per common share (up to EUR 695 million), in cash or in shares at the option of the shareholder, against the reserve retained earnings.

Shareholders will be given the opportunity to make their choice between cash and shares between May 7, 2012 and May 25, 2012. If no choice is made during this election period the dividend will be paid in shares. On May 25, 2012 after close of trading, the number of share dividend rights entitled to one new common share will be determined based on the volume weighted average price of all traded common shares Koninklijke Philips Electronics N.V. at Euronext Amsterdam on 23, 24 and 25 May 2012. The Company will calculate the number of share dividend rights entitled to one new common share, such that the gross dividend in shares will be approximately 3% higher than the gross dividend in cash. Payment of the dividend and delivery of new common shares, with settlement of fractions in cash, if required, will take place from May 30, 2012. The distribution of dividend in cash to holders of New York registry shares will be made in USD at the USD/EUR rate fixed by the European Central Bank on May 28, 2012.

Dividend in cash is in principle subject to 15% Dutch dividend withholding tax, which will be deducted from the dividend in cash paid to the shareholders. Dividend in shares paid out of earnings and retained earnings is subject to 15% dividend withholding tax, but only in respect of the par value of the shares (EUR 0.20 per share). This withholding tax in case of dividend in shares will be borne by Philips.

In 2011, a dividend of EUR 0.75 per common share was paid in cash or shares, at the option of the shareholder. Approximately 63% elected for a share dividend resulting in the issue of 22,896,661 new common shares, leading to a 2.4% percent dilution. The cash dividend was paid (EUR 259 million) against the net income for the financial year 2010. The remainder of the net income for the financial year 2010 has been retained by way of reserve.

The balance sheet presented in this report, as part of the Company financial statements for the period ended December 31, 2011, is before appropriation of the result for the financial year 2011.

5.6 Outlook

We are cautious about 2012, given the uncertainty in the global economy, and Europe in particular. In addition, we expect our 2012 results to be affected by the previously communicated restructuring charges and one-time investments aimed at improving our business performance trajectory, as part of the multi-year Accelerate! program.

Excluding these additional charges, we anticipate that underlying operating margins and capital efficiency will improve in the latter part of 2012.

5.7 Critical accounting policies

Critical accounting policies

The preparation of Philips financial statements requires us to make estimates and judgments that affect the reported amounts of assets and liabilities at the date of our financial statements. The policies that management considers both to be most important to the presentation of Philips financial condition and results of operations and to make the most significant demands on management s judgments and estimates about matters that are inherently uncertain are discussed below. Management cautions that future events often vary from forecasts and that estimates routinely require adjustment. A more detailed description of Philips accounting policies appears in section 12.10, Significant accounting policies, of this report.

Accounting for pensions and other postretirement benefits

Retirement benefits represent obligations that will be settled in the future and require assumptions to project benefit obligations and fair values of plan assets. Retirement benefit accounting is intended to reflect the recognition of future benefit costs over the employee s approximate service period, based on the terms of the plans and the investment and funding decisions made. The accounting requires management to make assumptions regarding variables such as discount rate, rate of compensation increase, mortality rate, return on assets, and future healthcare costs. Pension assumptions are set centrally by management in consultation with its local, regional or country management and locally appointed actuaries at least once a year. For the Company s major plans, a full discount rate curve of high quality corporate bonds (Bloomberg AA Composite) is used to determine the defined benefit obligation whereas for other plans a single point discount rate is used based on the plan s maturity. Plans in countries without a deep corporate bond market, use a discount rate based on the local sovereign curve and the plan s maturity. Relevant data regarding various local swap curves, sovereign bond curves and/or corporate AA bonds are sourced from Bloomberg. Changes in the key assumptions can have a significant impact on the projected benefit obligations, funding requirements and periodic cost incurred.

For a discussion of the current funded status, a sensitivity analysis with respect to pension plan assumptions, a summary of the changes in the accumulated postretirement benefit obligations and a reconciliation of the obligations to the amounts recognized in the consolidated balance sheet, please refer to note 29, Pensions and other postretirement benefits.

Accounting for income taxes

As part of the process of preparing consolidated financial statements, the Company is required to estimate income taxes in each of the jurisdictions in which it conducts business. This process involves estimating actual current tax expense and temporary differences between tax and financial reporting. Temporary differences result in deferred tax assets and liabilities, which are included in the consolidated balance sheet. The Company regularly reviews the deferred tax assets for recoverability and will only recognize these if it is believed that sufficient future taxable profit is available, including income from forecasted operating earnings, the reversal of existing taxable temporary differences and established tax planning relating to the same taxation authority and the same taxable entity. For a discussion of the fiscal uncertainties, please refer to the information under the heading Fiscal risks in note 3, Income taxes.

Provisions and Contingent liabilities

The Company and certain of its group companies and former group companies are involved as a party in legal proceedings, including regulatory and other governmental proceedings, and discussions on potential remedial actions, relating to such matters as antitrust laws, competition issues, commercial transactions, product liabilities, participations and environmental pollution. Since the ultimate disposition of asserted claims and proceedings and investigations cannot be predicted with certainty, an adverse outcome could have a material adverse effect on the Company s Consolidated financial statements.

The Company recognizes a liability when it is probable that an outflow of resources embodying economic benefits will result from the settlement of a present obligation and the amount at which the settlement will take place can be measured reliably. If the likelihood of the outcome is less than probable and more than remote or a reliable estimate is not determinable, the matter is disclosed as a contingent liability if management concludes that it is material.

In determining the provision for losses associated with environmental remediation obligations, significant professional judgments are necessary. The Company utilizes experts in the estimation process. Provisions for estimated losses from environmental remediation obligations are recognized when information becomes available that allows a reasonable estimate of the liability, or a component (i.e. particular tasks) thereof. The provisions are adjusted as new information becomes available and they are remeasured at the end of each period using the current discount rate.

Provisions on restructuring represents estimated costs of initiated reorganizations, the most significant of which have been approved by the Board of Management. A liability is recognized for those costs only when the Company has a detailed formal plan for the restructuring and has raised a valid expectation with those affected that it will carry out the restructuring by starting to implement that plan or announcing its main features to those affected by it.

Provisions on onerous contracts represent the lesser of the unavoidable costs of either fulfilling or exiting the related contract, and in which the costs to fulfill the contract exceed the benefits expected to be received under such contract. In determining the cost of fulfilling the contract, the payments due in the period in which the contract cannot be cancelled are considered, unless there is a lesser amount of penalty to exit the contract. Generally, unavoidable costs only include incremental costs related to the contract and exclude allocated or shared costs. Before a provision is established, the Company recognizes any impairment loss on the assets associated with that contract.

The Company provides for warranty costs based on historical trends in product return rates and the expected material and labor costs to provide warranty services. The provision is based on historical warranty data and a weighing of possible outcomes against their associated probabilities.

Provision for obsolete inventories

The Company records its inventories at cost and provides for the risk of obsolescence using the lower of cost and net realizable value principle. The expected future use of inventory is based on estimates about future demand and past experience with similar inventories and their usage.

Provision for bad debts

The risk of uncollectability of accounts receivable is primarily estimated based on prior experience with, and the past due status of, doubtful debtors, while large accounts are assessed individually based on factors that include ability to pay, bankruptcy and payment history. In addition, debtors in certain countries are subject to a higher collectability risk, which is taken into account when assessing the overall risk of uncollectability. Should the outcome differ from the assumptions and estimates, revisions to the estimated valuation allowances would be required.

Impairment of non-financial assets

Goodwill is not amortized, but tested for impairment annually and whenever impairment indicators require so. The Company reviews non-financial assets, other than goodwill for impairment, when events or circumstances indicate that carrying amounts may not be recoverable.

In determining impairments of non-current assets like intangible assets, property, plant and equipment, investments in associates and goodwill, management must make significant judgments and estimates to determine whether the recoverable amounts are lower than the carrying value. Changes in assumptions and estimates included within the impairment reviews and tests could result in significantly different results than those recorded in the consolidated financial statements.

The recoverable amount is the higher of the asset s value in use and its fair value less costs to sell, the determination of which involves significant judgment and estimates from management.

Goodwill is allocated to the cash generating units. The basis of the recoverable amount used in the annual (performed in Q2) and trigger-based impairment tests is generally the value in use. Key assumptions used in the impairment tests were sales growth rates, adjusted income from operations and the rates used for discounting the projected cash flows. These cash flow projections were determined using management s internal forecasts that cover an initial period from 2011 to 2015 that matches the period used for our strategic review. Projections were extrapolated with stable or declining growth rates for a period of five years, after which a terminal value was calculated. For terminal value calculation, growth rates were capped at a historical long term average growth rate.

The sales growth rates and margins used to estimate cash flows are based on past performance, external market growth assumptions and industry long-term growth averages. Adjusted income from operations in all units is expected to increase over the projection period as a result of volume growth and cost efficiencies. Please refer to note 9, Goodwill.

New Accounting Standards

For a description of the new pronouncements, please refer to the information under the heading IFRS accounting standard adopted as from 2012 and onwards in section 12.10, Significant accounting policies, of this report.

Off-balance sheet arrangements

Please refer to the information under the heading Guarantees in sub-section 5.2.9, Cash obligations, of this report and in note 25, Contingent liabilities.

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6 Sector performance

Corporate Technologies Corporate and Country Overheads Pensions Global Service Units Corporate Investments New Venture Integration Design

Our structure

Koninklijke Philips Electronics N.V. (the Company) is the parent company of the Philips Group (Philips or the Group). The Company is managed by the members of the Board of Management and Executive Committee under the supervision of the Supervisory Board. The Executive Committee operates under the chairmanship of the Chief Executive Officer and shares responsibility for the deployment of Philips strategy and policies, and the achievement of its objectives and results.

Philips activities in the field of health and well-being are organized on a sector basis, with each operating sector Healthcare, Consumer Lifestyle and Lighting being responsible for the management of its businesses worldwide.

The Group Management & Services sector provides the operating sectors with support through shared service centers. Furthermore, country management organization supports the creation of value, connecting Philips with key stakeholders, especially our employees, customers, government and society. The sector also includes pensions.

Members of the Board of Management and certain key

officers together form the Executive Committee

Also included under Group Management & Services are the activities through which Philips invests in projects that are currently not part of the operating sectors, but which could lead to additional organic growth or create value through future spin-offs.

At the end of 2011, Philips had 124 production sites in 26 countries, sales and service outlets in approximately 100 countries, and 121,888 employees.

Sales, IFO and Adjusted IFO 2011

in millions of euros unless otherwise stated

	sales	IFO	%	Adjusted IFO[1)]	%
Healthcare					