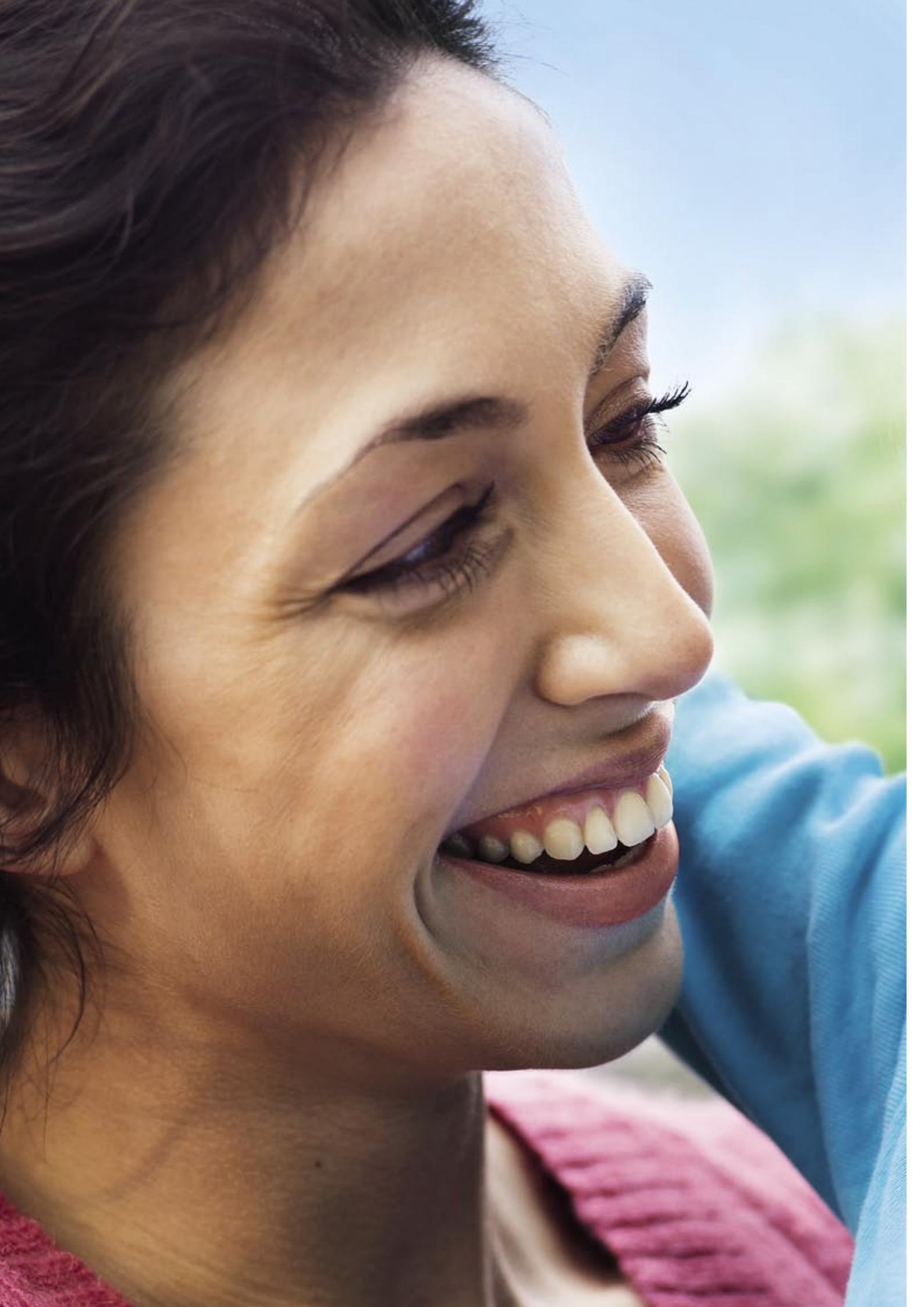
Simpler, stronger, greener

Sustainability Report 2007

PHILIPS



We make it easier to be green...

Live Earth
We entered a global partnership with Live Earth to help combat global warming. By joining forces with this largest global entertainment event in history, we inspired an estimated 2 billion people to lead a more energy-efficient lifestyle.

asimpleswitch.com
The asimpleswitch.com website is part of our campaign to encourage people to take simple steps to fight climate change, such as changing a light bulb. Visitors can make their personal "simple switch" pledge and calculate the resulting energy and cost savings.

Philips Green Products
Philips Green Products offer customers, users and society a significant environmental improvement in one or more of the Philips Green Focal Areas.

...and provid

Health & Wellbeing

We understand that whether it is getting the right care for their children or improving their own wellbeing, people want the best without the hassle. That is why we have created a range of solutions that can make better health easier to achieve.

At Philips we improve the quality of people's lives through the timely introduction of meaningful innovations. Using our expertise to simplify complex global challenges – the growing demands for energy efficiency and healthcare – we develop sustainable solutions for people in all markets.

e better care solutions

1

Simplified care
Our Ambient Experience CT brings a human design approach that can decrease sedation rates and increase workflow. Sedating a patient adds at least four hours to procedure time. Without sedation, most scans can be accomplished within 30 minutes.

Customer Satisfaction
Philips Ultrasound ranks #1 in overall service performance and all ultrasound systems for the 14th year in a row. Philips Patient Monitoring ranks #1 for the 8th consecutive year. Overall customer satisfaction is up thanks to our focus on patients and care providers.

Clinical collaboration
The best care requires collaboration among clinicians and specialists. With Philips iSite PACS doctors can access diagnostic images from any location in a hospital and make decisions as soon as a scan is completed.

About our report

Commitment to transparency

At Royal Philips Electronics we consider transparency about our sustainability activities a vital part of living up to our heritage of sustainable entrepreneurship.

The *Philips Sustainability Report 2007* is our tenth externally verified report. Our first environmental report was for the year 1998.

We expanded to sustainability reporting beginning with the year 2002 to cover the full spectrum of our social, environmental and economic performance.

This 2007 report demonstrates that sustainability is a business driver at Philips and is fully integrated in our strategy. Given our competencies and desire to improve lives with innovations that are important for society at large, we are focusing on energy efficiency and available and affordable healthcare. Therefore this report includes in-depth coverage of these key global challenges. The identification of these and other material issues is discussed on pages 20-22 and online.

Methods of delivery

In keeping with our brand promise of "sense and simplicity" this print report has been shortened to focus on the most material issues. Details on our employees, our environmental and economic performance, and our suppliers have been moved to our online report. Highlights of our performance in these areas can be found on pages 64-65.

The *Philips Sustainability Report 2007* is delivered as:

- A 74-page print document and
- An expanded online report, which includes the print document and additional chapters with specifics on our 2007 performance, as well as other information.

Both can be downloaded from our website www.philips.com/sustainability

Other information

Information on reporting standards, scope of the report, auditor policy, assurance assignment and assurance report from KPMG are included on page 67.

Print report

- About our report
- Interview with the President
- Becoming simpler, stronger and greener
- The Philips Way
- Philips and energy efficiency
- Philips and healthcare
- Highlights from our online report
- Appendix
- How to reach us

Online report

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- Our economic performance
- Our suppliers
- Sustainability trends and materiality mapping
- GRI Index

www.philips.com/sustainability

Contents

Forward-looking statements
This report 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. Examples of forward-looking statements include statements made about our strategy, estimates of sales growth, future EBITA and future developments in our organic business. By their nature, forward-looking statements involve risk and uncertainty because they relate to future events and circumstances and there are many 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, 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, changes in exchange and interest rates, changes in tax rates, pension costs, 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 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.

Statements regarding market share, including as to Philips' competitive position, contained in this document are based on outside sources such as specialized research institutes, industry and dealer panels in combination with management estimates. Where information 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.

Interviews
Philips does not necessarily agree with the opinions of external parties quoted in this report.

Interview with the President

With the "Vision 2010" strategic plan you've given stakeholders a clear blueprint of what you want Philips to be in 2010.

Yes, we have shared the next steps to grow the company further into a global leader in the areas of Healthcare, Lighting and Consumer Lifestyle. These steps aim to further position Philips as a market-driven, people-centric company with a strategy and a structure that fully reflect the needs of its customers and create value for shareholders.

How does sustainability fit in?

It is at the center of our strategy and rightfully so. At Philips we focus on our mission of improving the quality of people's lives. You can see this across the spectrum of our products and services. We aim to improve health and wellbeing, which are essential ingredients for creating sustainable societies. We also make a distinct contribution in energy efficient lighting. This is all right at the heart of sustainability.

So sustainability contributes to growth and value creation.

Absolutely. Initially people thought of it as a cost factor, which indeed it is when you treat it as an add-on. However, if it's designed into the way you do things from the beginning as it is here at Philips, it saves you money because you're operating more effectively. So today we recognize that sustainability offers significant business opportunities.

How do you go after those opportunities?

One way is through our EcoVision programs. Our latest EcoVision program, which is our fifth multi-year plan, sets targets to expand our revenues from Green Products, increase spending on Green Innovations, and improve the energy efficiency of our facilities.

We have been designing eco-friendly products for many years throughout our product range. Our products are designed to outperform their predecessors and competitors in terms of their ecological footprint. We want to provide people with Green Products that make it easy for them to contribute to saving our planet.

To do that, we have committed to doubling our investments to EUR 1 billion in Green Innovations in the next five years. We have already invested EUR 400 million in Green Lighting Technology during the last five years. You can see the results in our energy efficient lighting solutions that offer long lifetime and low energy consumption. This reduces end-of-life-issues along with greenhouse gas emissions.

"Our mission is at the heart of sustainability."

Gerard Kleisterlee President

So in terms of growth opportunities, we are convinced that combining the principles of economic growth and environmental stewardship will offer long-term rewards to all of our stakeholders.

Let's turn to healthcare. What differentiates Philips in this area?

The biggest advantage we can offer is through the close relationship between our Healthcare and Consumer Lifestyle activities. Firstly, the direction we are looking to extend to is wellbeing. Healthcare starts with prevention and a healthy lifestyle. Secondly, the most costly aspect of healthcare is late discovery and late treatment. Currently healthcare systems are reactive. We want to make a difference there as well – to help move healthcare from being reactive to being truly proactive.

How do you help bring about that shift?

We are moving to the direction of keeping people healthy in addition to our diagnostics and our other professional healthcare solutions. We can contribute by helping people live a healthy lifestyle. Our appliance activity does that. For example, our kitchen appliances can very much contribute to this by helping people prepare healthy meals and fresh juices. Or consider the connection between oral care and overall health. We can make a difference through maximizing the unique set of resources that we have in our company.

During 2007 you participated in stakeholder forums around the world. What have you learned from these conversations?

The purpose of these forums is not for participants to listen to Philips, but for Philips to listen to them. And for us, together, to envision solutions to the challenges we face in the areas of energy efficiency and healthcare.

From the Philips perspective, it's easier to make ourselves relevant in the energy efficiency discussion. It's at the heart of the debate around climate change. After all lighting accounts for 19% of global electricity use. As the world's leading lighting supplier our contribution to meeting this challenge is very straightforward.

And what did you learn from the healthcare stakeholder forums?

With healthcare there are multiple issues and more stakeholders. Our contribution overall is modest when you consider that we are just a relatively small part of the total healthcare value chain, in addition to doctors, hospitals, pharmaceutical companies, insurers, etc. So this is a more complex debate.

As a business we need to ensure that everything we do reflects what our customers want and need. We *must* make healthcare accessible and affordable for everyone, not only in advanced markets but also in new and emerging markets. Governments and insurers must also do their part. In turn we have to cooperate with governments, international organizations and non-governmental organizations in order to be effective.

I believe that a marriage of stakeholder needs and meaningful, cohesive policies will lie at the heart of successful strategies to meet the healthcare challenge.

Clearly sustainability requires an ever-increasing focus on the outside world. What does that mean in terms of the supply chain?

We have had a robust process in place since 2003 to involve our suppliers in sustainability. Our suppliers sign up to the same standards we adhere to and we conduct audits at supplier sites in new markets to ensure they do indeed live up to those requirements. If there are issues, we work with our suppliers to resolve them.

"We will continue to be proactive."

Multinational corporations have significant purchasing power and can make a large contribution by raising awareness, and encouraging and supporting suppliers in new, developing markets to raise their standards.

What about customers and consumers?

Retailers have an important role to play in educating consumers and we share that responsibility. We need to supply them with the tools they need in marketing and on the retail shelf. For example, we can provide information through point of sale material about the reduced total cost of ownership of our products that offer increased energy efficiency.

Our consumer website asimpleswitch.com shows that solutions for reducing energy consumption can be as simple as changing a light bulb. We supported the Live Earth concerts on July 7, 2007, to reach an estimated 2 billion people and inspire them to make a difference on the issue of climate change.

What do you believe is the role of leaders in sustainability?

Business leaders like political leaders in this context have the same job to do. We need to create awareness and come up with sustainable solutions for the problems we face as a society. Business will create the products and services; politicians need to provide the enabling conditions. At Philips we will continue to be proactive.

Industry for too long was seen as a source of problems. We need to correct that and show that we are part of the solution. When you are sustainable from the start, as I said, business is in a good position to contribute.

Look at what's happening in terms of demographics with population growth and aging. Now think about what that will mean to the world's resources. We need technological breakthroughs to deal with these challenges and ensure a sustainable future. Such breakthroughs can only come from industry. Businesses have R&D and make the investments in new technologies and new solutions – as we have done over the years and will continue to do.

What do you see ahead for sustainability at Philips?

With "Vision 2010" and the focus on our portfolio – Healthcare, Lighting and Consumer Lifestyle – sustainability will have an even more prominent place. It's a key element of how we do business. With this portfolio health and wellbeing is ever more at the heart of what we do. It's about quality of life and the quality of the environment we live in.

Becoming simpler, stronger and greener

Since our company was founded our mission has been to improve the quality of people's lives through the timely introduction of meaningful innovations. With growing concern about the environment and pressing social issues, sustainability has become even more important, evolving into a main business driver and strategic imperative.

We recognize that sustainability offers a world of opportunities to deliver value to individuals and communities around the globe, as well as to the company. We firmly believe that socially and environmentally sound behavior contributes to sustained profitable growth and value creation. This is reflected in our company strategy.

Strategic focus

As we strive to enhance the quality of people's lives, our 7 strategic drivers, detailed on pages 18-19, are helping us become a simpler, stronger and greener company. Number 6 states: "We are committed to sustainability and focus on making the difference in efficient energy use."

Clearly environmental stewardship and a commitment to energy efficient innovations will be a key characteristic of our development over the coming years. This will create value both for our planet and for our company. To sharpen our focus, we launched our latest EcoVision program in 2007, setting targets to further increase the energy efficiency of our products and facilities.

EcoVision4 targets

With EcoVision4, we have committed to:

- Generate 30% of total revenues from Green Products over the next five years (up from 15% in 2006);
- Double our investment in Green Innovations to EUR 1 billion by 2012; and
- Further increase the energy efficiency of our operations by 25% by 2012.

We are also engaging our employees, encouraging them to be environmentally aware at work and at home.

Making a positive impact

As the world leader in lighting, we can make a significant contribution to reduce global warming. A recent CO_2 abatement study by McKinsey identified energy efficient lighting as one of the most effective solutions for greenhouse gas reduction. Switching currently installed older lighting to the latest technology would save more than EUR 100 billion.

With our Green products it's possible to make "a simple switch" today. And the future promises more exciting developments as we drive for Green Innovations.

Caring for Climate

In July of 2007 our company attended the UN Global Compact Leaders Summit convened by UN Secretary-General Ban Ki-moon. Business leaders from 153 companies worldwide committed to speeding up action on climate change and called on governments to agree as soon as possible on measures to secure workable and inclusive climate market mechanisms after 2012, when the Kyoto Protocol expires. This call was made in a statement titled "Caring for Climate: The Business Leadership Platform." We are proud that Philips is a signatory to this statement.

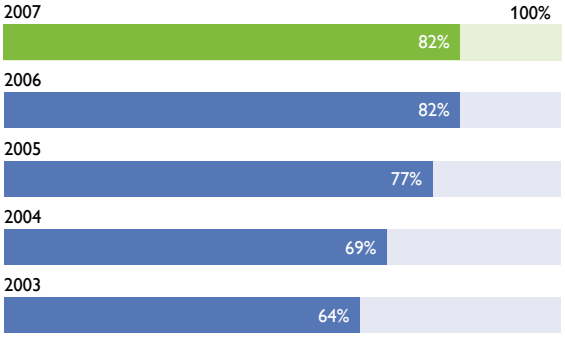
Innovations in energy efficiency and healthcare

In a meeting that brought together our businesses, Corporate Technologies, Product Development, Corporate Sustainability and others, we articulated our sustainable business strategy: "To become the recognized leader in key Philips global market opportunities relevant to society at large, by applying our company strengths." Therefore, in addition to energy efficiency we are focusing on available and affordable healthcare, and will continue to use our capabilities to make a positive impact on society at large.

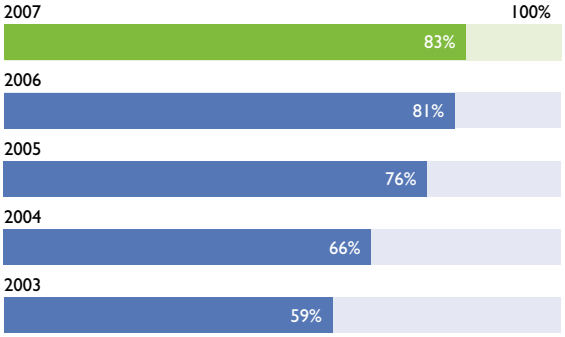
"Sustainability offers a world of business opportunities."

Barbara Kux Member Group Management Committee and Chair Sustainability Board

Philips' Dow Jones Sustainability Index scores
Total score



Philips' Dow Jones Sustainability Index scores
Social dimension



Making progress

Thanks to our teams around the world, and driven by our Sustainability Management Agenda and Key Performance Indicators (KPIs), we continue to make progress. During 2007 we focused on the following areas specified in our Sustainability Management Agenda:

Dow Jones Sustainability Index (DJSI)

We are proud to have achieved the position of DJSI supersector leader in our market sector. However, our total score of 82 did not increase compared to 2006. Our social score improved to 83 from 81 and our environmental score rose to 90 from 86. Our economic score was 75, down from 79 in 2006, in spite of the company's stronger financial performance. According to the Corporate Sustainability Assessment of SAM Research, which identifies the leaders for the DJSI, more transparency on our risk response strategy for non-financial risks is recommended.

In its detailed report on Philips, SAM Research noted:

"The early inclusion of sustainability in its strategic planning enabled Philips to identify two global challenges as key business drivers: energy and healthcare. In response, the company is refocusing its own activities and solutions around these themes in order to profit from new market opportunities and generate added value. For instance, the lighting division is developing answers to replace energy inefficient incandescent bulbs.

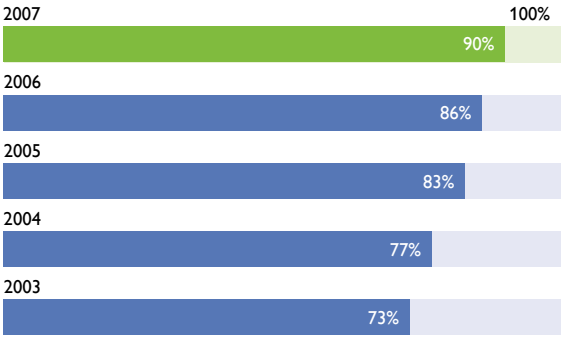
"To address the challenges with suitable products, Philips needs to identify early enough changes in the environment, understand the expectations of its stakeholders, integrate the findings into a product, have high regard for the environment and people in manufacturing, and finally reach the target customers. Sustainability thinking plays an important role in every aspect of this process.

Key Performance Indicators 2005-2007

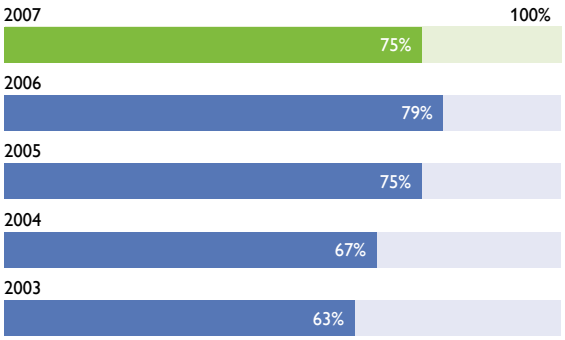
		2005 Actual	2006 Actual	2007 Target	2007 Actual
Business					
Sustainable business	Sales from sustainable business (Green Products), in %	-	15	20	20
	Number of new Green Flagships	46	57	60	53
Communication					
Internal communication	Sustainability messaging measured amongst employees as favorable (%)	62*	70*	75	72
External communication	Number of favorable clippings in top level printed media	322	453	500	493
Social					
Health and safety	Number of Lost Workday injury cases/100 FTEs	0.8	0.8	0.78	0.83
Diversity and inclusion	Women at executive level (%)	5	6	7	8
Human capital	Employee Engagement Index (% favorable)	59*	61	64	64
	People Leadership Index (% favorable)	55*	60	64	64
Reporting					
Supplier management	On-site assessments of identified risk suppliers (%)	-	98	100	100
DJSI rating	Overall increase 5% in 2007 score	-	82	87	82

* Including Semiconductors

Philips' Dow Jones Sustainability Index scores
Environmental dimension



Philips' Dow Jones Sustainability Index scores
Economic dimension



"Engaging stakeholders and monitoring customers' satisfaction enable Philips to better understand people's needs. Promoting innovation and R&D ensure the creation of unique products. The definition of clear environmental and social policies ensure sound manufacturing practices. Managing brands and a comprehensive code of conduct further support a proper market appearance. In all these areas, Philips achieves a score that is well above its industry's average."

EcoVision and Green Flagships

With the launch of EcoVision4, we further developed and built on our EcoVision environmental action programs.

Sales of Green Products increased to 20% of total sales, compared with 15% in 2006, representing an important part of our revenue stream.

The number of Green Flagship products declined with our current focus on Green Products and Green Innovations to drive growth. Ten years ago we introduced the Green Flagship concept. To drive a disciplined approach only individual top EcoDesigned products achieved Green Flagship status.

As more technologies and even complete product ranges could be identified as "green," particularly in Philips Lighting, we broadened our definition to "Green Products" in 2007.

We made good progress in communications but did not totally achieve our ambitious targets for the year, particularly on internal communication. In 2008 we will strengthen our approach to employee engagement by focusing on energy efficiency.

Social performance

We exceeded our diversity and inclusion target, with 8% woman at executive level, getting in sight of medium-term target of 10%.

With respect to health and safety, we saw a slight increase in lost working days, which will require more attention.

We refocused our social investment activities to reflect our business, directing our efforts on projects to upgrade lighting and healthcare initiatives that focus on children.

Auditing all identified risk suppliers

We audited all identified risk supplier sites, achieving our goal of 100% transparency.

We earned the Responsible Supply Chain Management Award in the Netherlands, ahead of 31 other multinational companies, listed on the AEX. According to a survey by the Association of Investors for Sustainable Development (VBDO), Philips achieved the highest score and also made the strongest improvement. Jury chairman Jan van der Kolk stated: "Philips differentiates particularly for its relatively high transparency and quantitative information on sustainable supply management in the 2006 report." Our online *Sustainability Report 2007* provides full details of our activities in this area.

The road ahead

We are committed to continuing to deliver on our Sustainability Management Agenda and KPIs, and on our EcoVision targets.

Sustainability Management Agenda 2008

In 2008 we will work to:

- Drive the implementation of the EcoVision program to achieve the 2008 results.
- Strengthen the energy efficient and Green Product approach at both Healthcare and Consumer Lifestyle, leveraging the experience of our Lighting sector.
- Make our supply chain fully compliant with the Electronic Industry Code of Conduct standard.
- Continue to engage employees on energy efficiency and carbon footprint awareness.

The Philips Way

Our company was founded in Eindhoven, the Netherlands, in 1891 to "manufacture incandescent lamps and other electrical products." Ever since then, we have been simplifying and enhancing people's lives with a steady flow of pioneering innovations, for instance in the fields of medical imaging, television, lighting, optical technology and integrated circuits. Today, we remain committed to building upon this rich heritage to make people's lives simpler, more enjoyable and more productive.

Vision 2010

In 2001 we started out on a journey to transform Philips into a focused, market-driven company capable of delivering sustained profitable growth, and so creating value for our stakeholders. Over the course of the intervening years, we have fundamentally repositioned Philips from a rather volatile, technology-focused, vertically integrated electronics company to an applications-oriented, customer-centric and more predictable company. This involved a massive capital re-allocation, away from cyclical technology businesses and toward expansion of our high-margin core businesses through acquisitions, innovation and brand injections, as well as returning capital to shareholders through tax-efficient share buy-backs and dividends. In 2007 we took another major step forward with the announcement of our Vision 2010 strategic blueprint.

Vision 2010 places the customer at the very heart of everything we do. Accordingly, we have realigned our entire organization around the needs we see in the marketplace. Effective January 1, 2008, we now have three sectors – Healthcare, Lighting and Consumer Lifestyle.

Insights and empowerment

Our mission is to improve the quality of people's lives through the timely introduction of meaningful innovations. In a world where complexity grows to touch every aspect of our daily lives, we will lead in bringing sense and simplicity to people.

Based on a deep understanding of what people really need and want, and delivering on our promise of simplicity, we empower our customers – both healthcare and lighting professionals and end-consumers – with solutions that are advanced, yet designed around them and easy to experience. Specifically, we address these needs and desires in the four domains of *my space, my body, my appearance* and *my mind*.

As well as expressing a commitment to eliminate unnecessary complexity and to deliver the meaningful benefits of technology, our "sense and simplicity" brand promise also defines how we want to be seen by all our stakeholders – open and transparent, approachable, easy to do business with.

Today, Philips is a much simpler company focused on the market, centered around the brand and driven by innovation. We see tremendous potential in both mature and emerging markets and leverage our competencies in design, technology and marketing to capture value from some of the major economic, social and demographic trends, e.g. the growing demand for better healthcare at lower cost, consumer empowerment, the rise of emerging markets and the need for energy efficiency.

As we strive to enhance the quality of people's lives, our 7 strategic drivers are helping us become a simpler, stronger and greener company.

Vision 2010 – ambition to significantly increase shareholder value

- Improve the EBITA margin of our current businesses to exceed 10%
  Through improved margin management, increased contribution from recent acquisitions, a better product mix, the effects of the organizational simplification and reduced corporate brand spend.
- Drive comparable sales growth at a minimum of 6% (compound annual sales growth) for the period 2008-2010
  Fuelled by organic growth, and through a specific focus on emerging markets and developing economies.
- Arrive at an efficient balance sheet by the end of 2009
  Through a combination of further value-creating acquisitions and continued return of capital to shareholders.
- Thanks to the combined effect of these measures, we expect EBITA per common share to more than double by 2010 from the 2007 level.

Management Agenda 2008

As a result of a thorough review of our 2007 achievements and remaining challenges, as well as our expectations for the development of the global economy and the competitive environment, we have adopted the following management agenda for 2008:

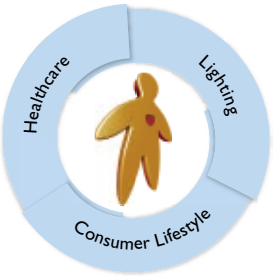
- Integrate and leverage recent acquisitions, delivering the anticipated return on investment
- Take decisive steps to structurally deal with unsatisfactory EBITA margins at Connected Displays
- Improve productivity as a driver of margin expansion
- Step up resource investment in emerging markets to accelerate growth in excess of 2x GDP
- Increase innovation focus in support of Philips' growth ambition
- Continue to drive a culture of superior customer experience
- Bring employee engagement to high-performance benchmark

Our 7 strategic drivers

1

We are a people-centric company that organizes around customers and markets

Vision 2010 positions Philips as a market-driven company with an organizational structure that reflects the needs of its customer base.



Our three new sectors, Healthcare, Lighting and Consumer Lifestyle, each address different markets, but have one thing in common – the customer is at the center.

By bringing together Medical Systems and our growing Home Healthcare Solutions business, for example, we can develop solutions that deliver value throughout the complete cycle of care – from disease prevention to screening and diagnosis to treatment, monitoring and health management.

And by combining CE and DAP, we will leverage our competencies to create competitive advantages in a challenging marketplace. Merging sales teams, for example, will create greater focus and reach within our chosen markets. Optimizing supply and service processes will improve customer-centric effectiveness. And combining consumer insights will enable us to deliver even more compelling value propositions.

2

We invest in a strong brand and consistently deliver on our brand promise of "sense and simplicity" in our actions, products and services

The 2007 wave of our brand campaign showcased a range of simplicity solutions that empower consumers, particularly families, to manage their health and wellbeing. These advertisements underscore the deep consumer knowledge and insights that set Philips apart in the healthcare industry.

By investing consistently in our brand – also through activities like our Simplicity Events – we are seeing its value increase significantly, as evidenced by our fourth successive rise in the annual Interbrand top 100.

3

We deliver innovation by investing in world-class strengths in end-user insights, technology, design and superior supplier networks

Technology continues to drive many of our innovations, and innovation is integral to everything we do. But to ensure it is relevant and meaningful, we take end-user insights as its starting point.

Product creation and development begins with an understanding of people's needs and aspirations. We make extensive use of our Experience Labs, where we can study people interacting naturally with our product concepts. If they find the concepts too complex, we make them simpler or go on to the next innovation.

The Philips Wake-Up Light is a new, medically proven wake-up solution based on the simulation of dawn. It emits light that gradually increases to the intensity you have selected, gently preparing your body to wake up. This "dawn light" positively affects your energy hormones, enabling you to rise naturally and easily, feeling energized and refreshed.

4

We develop our people's leadership, talent and engagement and align ourselves with high-performance benchmarks

In the 2007 edition of our annual Employee Engagement Survey, almost 100,000 Philips employees – from across all sectors and functions – were invited to answer the same 39 questions on leadership, management capabilities, alignment with Philips' vision, identification with the brand, and reward recognition.

The Employee Engagement Index figure increased to 64%, from 61% in 2006. We have set ourselves the goal of reaching the high-performance norm of 70% by 2009. So while we are on the right track, the remaining gap still needs to be closed.

5

We invest in high growth and profitable businesses and emerging geographies to achieve market leadership positions

We are well positioned to benefit from major trends that will determine global GDP development in the coming decade, i.e. the need of a growing and longer-living population for more and affordable healthcare, the need for energy-efficient solutions (e.g. for lighting) and developments in the consumer space. We are also well placed to realize profitable growth in emerging markets, while contributing to the sustainable development of these economies. We continue to pursue opportunities to make value-creating acquisitions that can further our growth ambitions. The acquisitions we announced in 2007, for example, strengthened or established our leadership positions in promising markets, or gave us access to new markets. The successful integration of Partners in Lighting International, Color Kinetics and Genlyte will significantly boost our global leadership position in the market for advanced lighting solutions, while the announced acquisition of Respironics puts us firmly at the forefront of the fast-growing market for home healthcare solutions. Now, the priority is to successfully integrate and leverage these acquisitions in order to capture their full value and so deliver the anticipated growth and margins.

6

We are committed to sustainability and focus on making the difference in efficient energy use

Global climate change, rising energy costs and pressure to meet targets on reduction of CO_2 emissions are major issues facing the world today. Addressing these imperatives and the opportunities they present will have a major impact on global business.

Philips has a long-standing commitment to providing solutions that improve people's lives and are environmentally sound. Now we are the industry leader in energy-efficient lighting with, for example, our state-of-the-art TL5 lamps and LED light sources, electronic gear, high-efficiency optics and energy-saving lighting controls.

We are aiming for our Green Products to generate 30% of total revenues by 2012, compared with 15% of group sales in 2006. This commitment is part of our latest EcoVision program, which aims to double our investment in green innovations to EUR 1 billion in the next five years and increase the energy efficiency of our operations by 25%.

During 2007 we launched our Green Logo, a simple tool to help consumers find Philips' Green Products in stores and make responsible choices.

asimpleswitch.com

7

We drive operational excellence and quality to best-in-class levels, allowing us to make strategic investments in our businesses

Philips Business Excellence (PBE) provides a holistic framework for assessing an organization's position relative to world-class performance, identifying strengths as well as improvement opportunities that support business objectives.

In few areas are the demands for manufacturing excellence higher than in the automobile industry. This drives our Automotive Lighting business, which has adopted a zero-defects policy – not as a philosophy but as a hard target.

Using the Philips Business Excellence program, our people at Automotive Lighting identify what improvements are needed, and formalize them in the management agenda. The policy is based on management attention and shop floor focus. Black Belts (process experts) and Green Belts (operational and tactical experts) lead improvement teams focused on product quality issues. Our Lighting Quality Improvement Competition provides a platform where the teams can share their experiences and learn from each other, as well as motivating and engaging our people.

Our sustainability focus

Key global trends and issues

Societal
Growing population in developing world
Aging population in developed world
Instability/terrorism
Emerging roles of industries and non-governmental organizations
Digital divide
Privacy
Rising attention on human rights
Business / Economics
New and emerging markets
Shift from West to East
Off-shoring/outsourcing
New business models
New technologies
Knowledge management
IP (infringement, licensing and enforcement)
Business integrity
Transparency/accountability
Health
Rising healthcare costs
Lack of access to affordable healthcare
Infectious diseases in developing world
Chronic diseases developing world
Threat of epidemics (Bird Flu, SARS, etc.)
Employee health and safety
Animal testing
Environment
Climate change
Clean air and water
Energy management
Limited natural resources
Take-back and recycling
Use of chemical substances in products
Waste management

Sustainability trends and relevant issues

We continuously look at the world around us to track key trends and material issues. We blend this outside-in perspective with internal analyses (including our company strategy and risk assessment processes) to determine the issues most relevant for our company and those where we can make a positive contribution to society at large.

We review trend analyses from a variety of sources, including the World Bank, World Business Council for Sustainable Development, World Economic Forum and World Health Organization, as well as our own research. As a member of organizations like the World Business Council for Sustainable Development and the Electronic Industry Code of Conduct, we participate in meetings and task forces, bringing new learning to bear. Our work also involves tracking topics of concern to governments, regulatory bodies and non-governmental organizations, and following the resulting media coverage.

Stakeholder engagement

To gain additional outside perspective on sustainability trends and global issues, we engage our stakeholders in a variety of ways. We strengthened our approach to stakeholder engagement in 2007 with, among other activities, a series of Philips Forums and our first Sustainability Innovation Day event.

Philips Forums

Our stakeholder outreach program includes genuine dialogue with small groups of opinion leaders and relevant stakeholders at a series of events we call Philips Forums. In 2007 we held sessions in Kuala Lumpur, Singapore, Tokyo and the United States, and we plan to conduct additional forums in 2008.

The purpose of the Philips HealthCare and EnergyCare Forums is to create an environment in which leading stakeholders and the company's top management can

engage in a two-way exchange of ideas and opinions on issues of mutual interest, social relevance and global importance.

Based on societal trends within the healthcare and energy sectors, the aim is to share expertise and co-create solutions that will make a difference to future generations.

Sustainability Innovation Day

We discussed projects we are exploring with key stakeholders at Sustainability Innovation Day at our Corporate Research Exhibition in May 2007. Originally launched in 1959 as an internal event intended to help researchers from different labs find synergies in their work, in 2001 Philips businesses began bringing strategic customers to the event and extending invitations to other key external stakeholders in the following years.

Among the guests on Sustainability Innovation Day were members of government, academia and non-governmental organizations. Inviting outside parties to this event is an example of our Open Innovation model. We strongly believe that partnerships are a lot stronger than just doing things on our own. So outside feedback is very important to us. After seeing innovations we are exploring in healthcare and energy, attendees shared their insights and challenged the company to ensure that environmental and social issues are at the forefront of the innovation process.

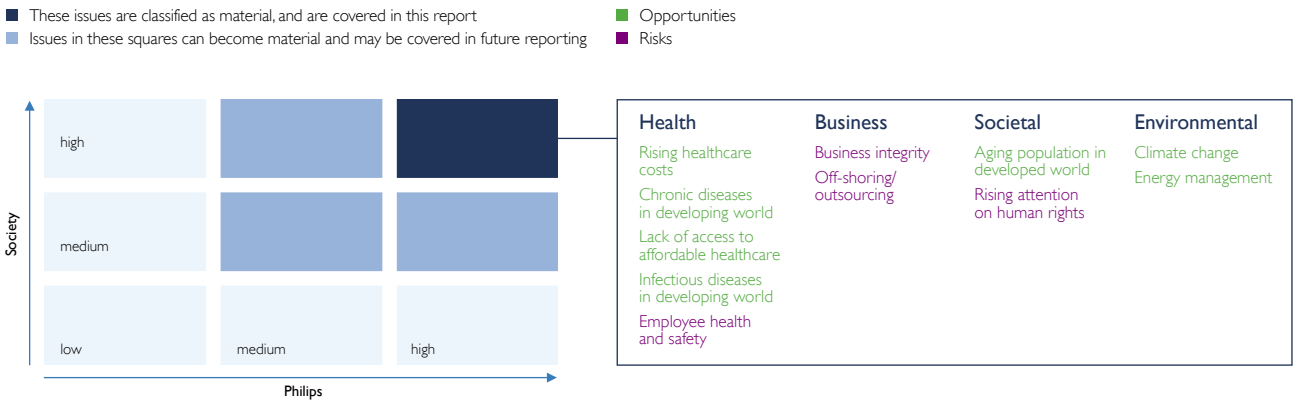
Key material issues

To identify the key material issues we use the mapping approach shown below, which plots the material issues on a scale from low to high in terms of the:

- level of concern to society and stakeholders, versus
- impact on Philips, or
- level of control or influence we can have on an issue through our operations and products/solutions.

The overview of material issues illustrated here includes both risks and opportunities. Our primary focus in this report is on business opportunities – to show how we can play a positive role in meeting the sustainability challenges we face globally.

Materiality matrix
The mapping approach



We also recognize that opportunity brings responsibility and requires managing risk. Detailed information on our General Business Principles, Supplier Sustainability Involvement Program, and our approach to risk management and control can be found in our online *Sustainability Report 2007* and our *Annual Report 2007*.

Based on global trends, stakeholder input and our company strengths, we develop our strategy and vision, as well as the programs and policies to drive the implementation of our strategy.

Our focus

We want to become the recognized leader in key Philips global market opportunities relevant to society at large, by applying our company strengths. As a result, we focus on energy efficiency and healthcare.

Healthcare

The area of healthcare is clearly of essential importance. Every human being should have access to affordable healthcare of decent quality. To achieve this goal will require a huge effort. As a result, healthcare will be a very important driver of economic development over the coming decades.

Businesses, government, insurers and healthcare institutions will have to work together to find innovative solutions. For example, we need to shift from costly treatment at a late stage of disease to prevention and early detection. Prevention can be increased by healthier lifestyles and a cleaner environment. Remote patient management can help us to bring healthcare to areas where traditional healthcare is not available. At Philips this means focusing on the full cycle of care, which is described beginning on page 46.

Our heritage of understanding how people react to technology, combined with our deep clinical knowledge, puts us in a unique position to address the challenges of contemporary healthcare systems.

The pursuit of personal wellbeing is a universal trend, equally relevant in both mature and emerging markets. Our focus is shifting from products to experiences or atmospheres that reinforce healthy lifestyles, as illustrated by our ambient experiences and our emphasis on entertainment and wellbeing in the home and beyond.

Energy efficiency

As for energy management, climate change is one of the most pressing issues of our time. At the same time, we know that energy resources, so necessary for development, are scarce.

Energy efficiency helps to address both challenges. As the number one lighting company in the world, Philips is taking the lead in the promotion of innovative, energy efficient lighting solutions in houses, streets, offices, shops and cars. And we are strengthening the energy efficient and Green Product approach at both Healthcare and Consumer Lifestyle, leveraging the experience of our Lighting sector. You can find full details beginning on page 26.

EcoVision4

In 2007 we launched our latest environmental action program, EcoVision4.

We were at the forefront back in 1994 when we instituted a disciplined approach to environmental improvement with our first program, which set a series of measurable targets. At the same time, we introduced our EcoDesign process, which deals with all aspects of the product creation process. In 1998 we began our drive to develop Green Products. Since then we have continuously raised the bar with the ambitious goals of our subsequent programs, including EcoVision4.

EcoVision4 targets

With EcoVision4, we have committed to:

- Generate 30% of total revenues from Green Products over the next five years (up from 15% in 2006);
- Double our investment in Green Innovations to EUR 1 billion by 2012; and
- Further increase the energy efficiency of our operations by 25% by 2012.

Green Products

Philips Green Products offer customers, users and society a significant environmental improvement in one or more of the Philips Green Focal Areas:

Energy efficiency | Packaging | Hazardous substances | Weight | Recycling and disposal | Lifetime reliability

We use the Life Cycle approach to determine a product's overall environmental improvement. The Life Cycle Assessment calculates the environmental impact of a product over its total life cycle (raw materials, manufacturing, product use and disposal). The result of such a calculation is an Eco-Indicator.

The score of a given product in a Green Focal Area is significantly better when it is 10% better compared to the reference product, which can be a competitor, predecessor or other product in the particular product family.

Green Innovations

The need for Green Innovations is clear and we are working to ensure that we get the maximum results from our efforts to stimulate innovation. Corporate Technologies – which includes Corporate Research, Philips' Incubators, Intellectual Property & Standards, campuses in India and China, as well as Applied Technologies – feeds our innovation pipeline.

Our goal is to develop true breakthroughs that benefit society and create value for the company and our stakeholders. We will do that through our investment in Green Innovations, concentrating on our main areas of expertise.

We recognize that innovation is not limited to inventions brought about by basic research. Progress can also be driven by the development of original applications of technologies that already exist. One example is our energy efficient urban lighting solutions. In addition to Green benefits, these lighting architecture solutions improve safety, comfort and atmosphere.

We also know that we have to be flexible to truly maximize the value from our innovation efforts. Not every promising idea can be nurtured within the environment of our established businesses – sometimes because the idea is too much of a break-away, sometimes because the expected returns or scale up are too slow for our global businesses. We would be destroying value if we just left those technologies on the shelf. That's why we have set up three Incubators – to develop these technologies in

a separate, entrepreneurial environment that measures performance in terms of growth, not earnings.

After nurturing and developing these ideas for a few years, successful incubator initiatives make it into new businesses, often within Philips, but we have also spun out some of them as independent companies. Society at large profits, because promising technologies do not rust on the shelves and can be developed into new business. Philips profits, because the incubators allow us to extract more value from our R&D efforts.

Operational energy efficiency

To improve our operational energy efficiency, and reduce the associate CO_2 emissions, we needed a solid baseline from which to compare our improvement in the coming years. So during 2007 we worked to establish a clear view of our company's operational carbon footprint, applying the Greenhouse Gas Protocol. Developed by the World Business Council for Sustainable Development and the World Resources Institute with extensive review from stakeholders around the world, this is the most accepted standard to calculate greenhouse gas emissions.

Our operational carbon footprint

We focused particularly on those areas we can directly influence, for which we have set reduction targets. Our operational carbon footprint includes:

- Direct emissions from our manufacturing processes and non-manufacturing facilities.
- Indirect emissions from purchased electricity.
- Other indirect emissions that we can influence directly: logistics and business travel.

Our operational footprint does not include, among others, the following elements of indirect impact:

- Production of purchased materials and outsourced manufacturing activities. However, we are starting to work with some of our key suppliers to improve their operational energy efficiency. (Details are available in the section on "Our suppliers" in our online report.)
- The use of our products. By far the most significant impact on global warming is from the use of our products. Based upon preliminary estimates, the carbon footprint for use of our products is more than 300 million tons of CO_2 equivalents, most of which relates to lighting products. For perspective, our operational carbon footprint is less than 1% compared to the impact of the usage of our products. This is why we have sharpened our focus on Green Products and Green Innovations.

Additional details on how we calculated our operational carbon footprint can be found on pages 68-96.

Calculating our carbon footprint is a complex exercise. Not all source data are directly available, while other data have been measured for 10 years (in our manufacturing facilities, for example) and are highly reliable. Some data were incomplete and had to be extrapolated or converted from other source data or estimated. We will continue to work to further improve the data, using 2007 as a solid base for reporting our improvements through 2012.

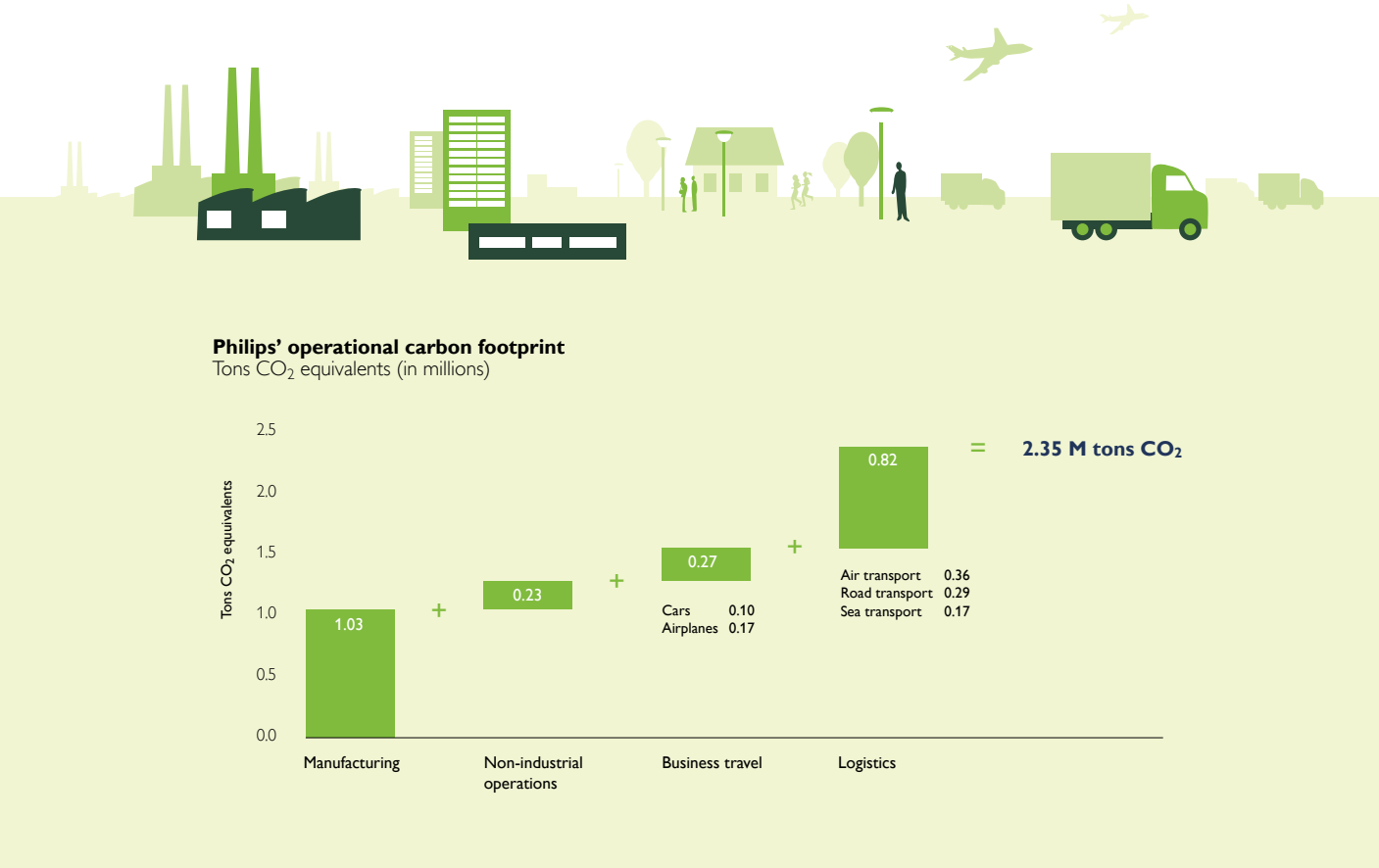
Based upon the available data, we calculated our total operational footprint to be approximately 2.35 million tons CO_2 equivalents.

For each area we have developed action programs to drive energy efficiency and associated CO_2 reductions.

Manufacturing

In manufacturing we have targets to improve energy efficiency as part of our EcoVision III (2005-2009) program. Currently we are expanding this to specific targets for each sector through 2012.

"We are commited to reduce our operational carbon footprint."



Non-industrial facilities

For our non-industrial facilities (offices, warehouses, etc.) we are focusing on upgrading our lighting systems.

Business travel

We are strengthening our programs to reduce the impact of business travel, including videoconferencing, low carbon car rentals and Green car leasing. (See the section on "Our suppliers" in our online report.)

Logistics

Air transport accounts for the majority of the total CO_2 emissions related to logistics. We are putting programs in place to use the type of transportation that has the lowest CO_2 impact per kilometer. (Please see "Our suppliers" in our online report.)

I can make a difference now

Philips and energy efficiency

"I knew there was something going on about climate change, but it seemed so complicated. What possible difference could just one person make? I found out at the Live Earth concert and the Philips asimpleswitch.com site. One individual truly has power! By simply changing four old light bulbs in my home to energy savers, each year our atmosphere will be spared up to 160 kg of CO_2 – and my energy bill will be reduced by EUR 48. And if I tell 10 friends, that power grows exponentially."

Our www.asimpleswitch.com site shows how a simple act can have a powerful impact.

Climate change: complex and unequivocal

Hardly a day passes without media headlines about climate change.

Al Gore's film *An Inconvenient Truth* became an Academy Award winner in February. Leonardo DiCaprio and the former US Vice President announced the Academy's green initiative, which includes a variety of energy-saving strategies.

July brought Live Earth, the largest global entertainment event ever held. This 7-continent, 24-hour music event broke on July 7, 2007. The concerts attracted TV, radio, Internet and live audiences, and generated attention and discussion around the world, engaging an estimated audience of 2 billion people on the issue of climate change.

"Extensive climate changes may alter and threaten living conditions."

The Norwegian Nobel Committee announced in October that the Nobel Peace Prize for 2007 would be shared by the Intergovernmental Panel on Climate Change (IPCC) – a scientific intergovernmental body set up by the World Meteorological Organization and the United Nations Environment Programme – and Al Gore. The Committee said the joint award was "for their efforts to build up and disseminate greater knowledge about man-made climate change, and to lay the foundations for the measures that are needed to counteract such change."

Indeed the Committee called for sharper focus on the issue, noting: "Indications of changes in the earth's future climate must be treated with the utmost seriousness, and with the precautionary principle uppermost in our minds. Extensive climate changes may alter and threaten the living conditions of much of mankind. They may induce large-scale migration and lead to greater competition for the earth's resources. Such changes will place particularly heavy burdens on the world's most vulnerable countries. There may be increased danger of violent conflicts and wars, within and between states."

Rising high

Sea level
Average global sea level is projected to rise by 28-58 cm

20-30%

Gone forever
20-30% of species are likely to face an increased risk of extinction

Declining

Melting snow
Glaciers retreated significantly during the 20th century

Changes already seen

In November the IPCC 4th Assessment Report (AR4) – "Climate Change 2007" – was completed. "Unequivocal" is the word the IPCC now uses to describe the warming of the climate system. Trends towards more powerful storms and hotter, longer dry periods have been observed and are assessed in the report.

Closing out the year was the United Nations Climate Change Conference in Bali. Hosted by the Government of Indonesia, this two-week event brought representatives of over 180 countries together with observers from intergovernmental and non-governmental organizations, and the media.

The effects of change

Explaining climate change science, the United Nations says: "Human activity – particularly the burning of fossil fuels – has made the blanket of greenhouse gases around the earth 'thicker.' The resulting increase in global temperatures is altering the complex web of systems that allow life to thrive on earth, such as cloud cover, rainfall, wind patterns, ocean currents, and the distribution of plant and animal species."

What the future holds

The UN says that "even the minimum predicted shifts in climate for the 21st century are likely to be significant and disruptive. Scientific understanding and computer models have improved recently and many projections can now be made with greater certainty… Predictions of future climate impacts show that the consequences could vary from disruptive to catastrophic."

Severe storms and floods are likely along the world's coastlines, while other areas will suffer prolonged draught. Food supplies could dwindle. With higher temperatures diseases like malaria, which already kills 1 million people a year, can expand their range. And it's expected that the poorest communities will be the hardest hit. Yet, as UN Secretary-General Ban Ki-moon points out, "Global warming impacts everyone regardless of national borders." Climate change "doesn't care if you are coming from developing or industrialized countries."

What we believe

As a global business we are acutely aware of our duties as a citizen of the world and the role we can play in improving people's lives.

We believe concerted action in climate change is a social responsibility. Realizing real and immediate differences in the way the world thinks and acts to reduce its ecological footprint is our passion. We believe future generations are entitled to a healthy planet.

At Philips we meet the energy efficiency challenge with our Green Products and by inspiring individuals to make simple changes that can have profound results. We seek to facilitate new solutions for change to drive responsible energy practices.

Providing simple solutions

While many of the necessary building blocks are falling into place, winning the war against climate change still requires a change of behavior and attitude among every single consumer, whether acting personally or professionally. Bringing that about will demand concerted action from everyone involved in the consumption of energy, from industry, energy suppliers, governments, non-governmental organizations and consumer groups.

The world may indeed face an energy problem, but we prefer to see Philips as part of the energy solution. As the world's leading lighting supplier we can have a big impact on energy efficiency and the resulting carbon dioxide emissions. Since we invented the energy saving compact fluorescent light bulb in 1980 we have continued to develop energy efficient lighting solutions that offer significant savings in energy, expense and CO_2 emissions.

Consider the numbers

Lighting accounts for 19% – or nearly one-fifth – of all electricity used in the world. That's because much of the lighting currently installed is technology that dates back a century. With this old inefficient lighting, 95% of the energy is wasted in heat, with a mere 5% generating light.

Some 75% of all lighting is used in professional applications like street lighting and buildings, while 25% is used in homes.

If new efficient lighting technologies were adopted globally, the world could achieve an energy saving of 40%. This would save EUR 106 billion in energy costs per year. This is equivalent to 555 million tons of CO_2 or 1.5 million barrels of oil a year.

Selling these lighting solutions is not only good for Philips, it's also good for people and the planet.

Beyond lighting

Of course, we also focus on energy management in our Consumer Lifestyle products.

People wonder about those big TVs with little red standby lights that never turn off. Ten years ago that same red light used 8 or 9 watts of standby power. We've brought that down to 0.15 watts in the majority of the TVs we will introduce in 2008.

In recognition of this, the Consumer Electronics Association honored Philips with a 2008 International CES Best of Innovations Design and Engineering Awards in an important new category: Eco-Design and Sustainable Technology. Our 42-inch 1080p Pixel Plus 3HD LCD HDTV – a typical TV in our 2008 product range – offers significant environmental benefits, including best-in-class standby energy consumption.

We are working to further strengthen the energy efficient and Green Product approach at both our Healthcare and Consumer Lifestyle sectors.

Energy efficiency lies at the heart of our business. It's one of the practical ways we deliver on our brand promise of "sense and simplicity."

#1

Leadership position
We're the world's leading lighting supplier

Delivering

Energy efficiency
Providing energy-efficient solutions is one of the ways we deliver on our brand promise

19%

Nearly one-fifth
Lighting accounts for 19% of global electricity use

Getting the word out

Our research tells us that people want to be good citizens. They want to reduce their carbon footprint. But they are not necessarily willing to sacrifice their gratifying consumer lifestyle.

Our response is simple. "Make a start with lighting."

One of our big initiatives in 2007 was continuing our call to action to get the world to switch from old to new lighting technology.

We believe our job is to make the transition to energy saving lighting smooth and as easy as possible for our customers – whether they be governments, businesses or homeowners. We have public awareness programs running in all major regions, launching initiatives in Hong Kong, China, Washington, DC, and California. This is in addition to the energy efficiency awareness initiative launched in Europe in 2003.

Making a "simple switch"

In July we launched our global consumer campaign called asimpleswitch.com, showing that solutions for reducing energy consumption can be simple and actionable without compromising on quality of life.

By partnering with The Alliance for Climate Protection and the global Live Earth concerts on July 7, 2007, we helped inspire more than 2 billion people to take simple steps, like changing a light bulb, to lead a more energy efficient life.

Part of the campaign is a consumer website www.asimpleswitch.com, launched on July 4, 2007. Visitors to the Live Earth concerts and the Live Earth and MSN websites were invited to record a personal "simple switch" pledge either online or via text messaging.

We are tracking these collective pledges to change to energy efficient lighting and calculating the resulting energy and costs savings on the asimpleswitch.com website. Nearly 3.4 million switches had been pledged at year end.

Former US Vice President, creator of *An Inconvenient Truth* and Live Earth spokesperson Al Gore said in a message to Philips employees: "Together we can continue to get out the word that there are many simple and accessible solutions that help reduce our energy consumption and cut global warming pollution."

This outreach is indeed working. We see that the switch in residential lighting is going very fast because it's the most "simple switch."

Philips Green Products

We will use the Philips Green logo (seen on the balloon in the accompanying photo) to identify our Green Products, making it simple for our customers and end-users.

Shaping public policy

Because we moved early, the Philips voice is a leading part of a global choir.

Europe: Saving 20% in 2020

The European Commission has been urged by EU leaders to "rapidly submit proposals" to get 490 million citizens in 27 member states to switch bulbs. The EU action plan for energy efficiency calls for reducing primary energy use by 20% in 2020.

"This historic legislation makes a much-needed 'down payment' on curbing global warming."

The Commission's Directorate-General for Energy and Transport has stated: "Making improvements to lighting is one of the fastest ways to cut energy bills, and one of the easiest ways to save energy in buildings. Low energy bulbs, which are now readily available in shops, use less than a quarter of the electricity of a standard light bulb and last up to 15 times longer. According to estimates, replacing bulbs can save an average household around EUR 100 every year. "

Initial priority products for energy performance standards include office lighting and street lighting, followed by incandescent lamps.

Australia: Eliminating inefficient bulbs

Australia's government is banning old-style bulbs within three years.

The Americas: Making the switch

In the Americas both Cuba and Venezuela have their switch programs. And at the end of 2007 the US enacted historic lighting efficiency legislation.

The comprehensive "Energy Independence and Security Act of 2007" contains a lighting efficiency section that will dramatically change consumer lighting in the US by setting aggressive energy efficiency standards for most of the more than 4 billion screw-based lights in the country.

The legislation will effectively ban the inefficient incandescent bulb. This segment of the market will move to lamps equal to or more efficient than our Halogená Energy Saver lamps, which are already on the market. Other alternatives include compact fluorescents and solid state lighting (LEDs). The phase out of inefficient lamps is slated to begin on January 1, 2012, and will be completed within two years.

The legislation will reduce Americans' electric bills up to $18 billion annually, and reduce electricity consumption equal to that generated by 23 nuclear power plants or 80 coal burning plants.

Other provisions include efficiency standards for reflector lamps and metal halide fixtures and a requirement that the federal government purchase only highly efficient lighting products.

This US legislation came just one short year since we issued our call to action in Brussels on December 7, 2006, urging governments around the world to adopt policies to remove inefficient lighting products from the market by 2016.

With the creation of the Lighting Efficiency Coalition on March 14, 2007, Philips, key members of the US Congress and five major environmental organizations echoed this call to action at the National Press Club. The environmental organizations – the Alliance to Save Energy, American Council for an Energy Efficient Economy, Californians Against Waste, Earth Day Network and the Natural Resources Defense Council – advocated this legislation and negotiated its specifics.

"Of the many initiatives and ideas that have been brought to the Alliance to Save Energy during our 30-year history, none has offered – or will deliver – the energy savings provided through the coalition effort to phase out inefficient, incandescent bulbs in the United States," said Kateri Callahan, President of the Alliance to Save Energy.

4 billion

Incandescent light bulbs
This segment of the US market will move to energy saving lamps

20%

in 2020
The EU is calling to cut energy use by one-fifth

"In addition to helping American consumers and businesses, this historic legislation makes a much-needed 'down payment' on curbing global warming and confronting other critical energy issues, including national energy security and the health of our economy."

Spreading the message

During the course of 2007, Philips executives took the company's call to action to participants at meetings on climate change and energy efficiency all over the world, including Berlin, Brussels, Delhi, Geneva, São Paulo, Seattle and Singapore, to name just a few.

They reiterated that the time for change is now, with the combined pressures of global warming, rising energy prices and security of the energy supply. Further, energy efficiency can help drive economic growth in advanced as well as in new and emerging markets.

The Lisbon Council for Economic Competitiveness and Social Renewal – a think tank and policy network committed to defining and articulating a mature strategy for managing current and future challenges – convened the Climate Change Action Group in June. Among the participants was a senior expert from Philips.

With a strong focus on technology and innovation, the Climate Change Action Group seeks to stimulate solution-oriented policy debates, encouraging the development of a strong public policy environment that will encourage sustainable 21st century business models.

We also have established a partnership with IUCN aimed at increasing awareness on climate change and solutions to combat it. Also known as the World Conservation Union, IUCN brings together 83 States, 110 government agencies, more than 800 non-governmental organizations, and some 10,000 scientists and experts from 181 countries in a unique worldwide partnership.

IUCN's work includes giving policy advice and technical support to governments, United Nations organizations, international conventions and other groupings such as the G8 and G77, as well as providing technical support for drafting environmental laws and natural resources management strategies. The organization also has the official status of Observer at the United Nations General Assembly.

"Making improvements to lighting is one of the fastest ways to cut energy bills, and one of the easiest ways to save energy in buildings."

© United Nations

Appealing to the world

Philips repeated our call to action on climate change during the UN Climate Change Conference in Bali. The appeal describes specific steps that industry and government can take to reduce CO_2 emissions and still maintain economic growth. As the world leader in lighting, we are encouraging developed and developing countries to embrace energy-efficient lighting solutions and accelerate the replacement of outdated polluting technologies.

High time for a switch

New energy efficient and environmentally friendly lighting products are available now. We believe it is high time for a switch in light of how serious the climate crisis is.

Harry Verhaar, Senior Director, Energy & Climate Change for Philips Lighting, said: "We hope governments will take steps towards introducing concrete environmental performance targets for buildings and roads and labeling schemes, as well as offering financial incentives that overcome initial investment hurdles. Finally we hope measures will be taken to stimulate further green procurement in energy efficient lighting for public buildings, schools and roads."

Calling climate change "the moral challenge of our generation," UN Secretary-General Ban Ki-moon said "the eyes of the world" were on ministers and heads of state in Bali. "Succeeding generations depend on us," he said. "We cannot rob our children of their future."

> "Succeeding generations depend on us."

Business input is indispensable

Executive Secretary of the United Nations Framework Convention on Climate Change Yvo de Boer called for the active engagement of the international business community in the talks on a future climate change deal.

"You are the key to a low carbon future. If Bali will do what I hope it will do, we are facing the enormous challenge of shaping a post 2012 climate change deal in only two years time. Your input is indispensable to frame a deal that is not only effective in terms of emission reductions, but also makes economic sense."

All countries

Replace outdated lighting
We encourage developed and developing countries to embrace energy-efficient solutions

Security

Improving lives
Effective lighting produces a sense of wellbeing

50%

Less energy
Our innovative street lighting cuts energy use in half

Concepts for sustainable cities

During the year we unveiled the results of our city.people.light2007 research, carried out with leading architects, lighting designers and urban planners. The findings reveal that sustainability is a key concern for urban life and lighting in the coming decade, and needs to be addressed to ensure sustainable cities as well as to respond to climate change. At the City.People.Light Forum, held in Rotterdam in May, we demonstrated that the development of energy efficient lighting solutions can go hand in hand with the development of socially sustainable lighting solutions to improve safety and wellbeing in urban environments.

Research into urban life and the role of city lighting has never been more important. A century ago less than 10% of the world's population lived in cities. Today, that figure has soared to more than 50%. And by 2050, it is expected to be over 75%. Many of these city dwellers will live in mega-cities in Asia and South America. Cities such as Shanghai (with a population of over 18 million) are already more populous than many European countries.

Sustainable lighting solutions
We are at the forefront of energy efficient urban lighting solutions. In 2005 we launched the world's most energy efficient high quality street lighting system called CosmoPolis. Since then more than 50 cities around the world have started installing this system, which cuts energy consumption by 50% and also reduces electricity costs. It also improves the quality of light, producing a greater feeling of security and wellbeing.

In the new area of solid-state lighting we are also leading the way. Solid-state lighting increasingly allows city authorities to combine socially sustainable lighting plans with drastically reduced energy and maintenance costs.

The symbolic Bosphorus Bridge in Istanbul, below, has been illuminated using our LEDs and luminaires (complete lighting fixtures). The installation consumes 50% less energy than previously required.

Getting to zero



Our Solid-State Lighting Solutions headquarters merges the green design with innovative uses of its energy efficient LED lighting technology.

Buildings represent 40% of the world's energy demand. And this is projected to rise substantially as population grows, moves to cities and becomes more affluent. Clearly there is tremendous potential for reducing energy consumption and CO_2 emissions in this sector.

To help do just that, we have joined forces with eight other members of the World Business Council for Sustainable Development (WBCSD) in the organization's Energy Efficiency in Buildings (EEB) project. This industry-only three-year initiative envisions a world where buildings consume zero net energy.

The future is now

While we at Philips are indeed looking to the future, we also are focused on what we can do today. Our own Solid-State Lighting Solutions headquarters in Burlington, Massachusetts, US, was officially unveiled in December 2007. This 50,000-square foot building merges the principles of green design with innovative uses of its energy efficient LED lighting technology throughout.

The space was designed to meet high standards of environmental design, including the use of LED lighting wherever possible, with a plan to be entirely LED-lit in the future. The central lighting system incorporates wall switch occupancy sensors to eliminate wasteful light. Energy Star-rated appliances are used throughout the space, and water- and energy-saving devices are installed in the restrooms. This effort aligns with our latest EcoVision program, which aims to increase the energy efficiency of our operations by 25% in the next five years, among other goals.

Clinton Climate Initiative

We are partnering with the Clinton Climate Initiative (CCI). CCI is working with the C40 Large Cities Climate Leadership Group – an association of large cities dedicated to tackling climate change – to develop and implement a range of actions that will accelerate greenhouse gas emissions reductions.

CCI's website points out: "With cities contributing approximately 75% of all heat-trapping greenhouse gas emissions to our atmosphere, while only comprising 2% of land mass, large cities are critical to winning this fight and slowing the pace of global warming." The goal is to enable CCI partner cities to reduce energy use and CO_2 emissions. Lighting can make a significant contribution to achieving this ambition.

Powerful partnerships

We partner with the World Green Building Council and the US Green Building Council, reaching key members of the building industry. Other partnerships in North America include the Alliance for Sustainable Built Environments, the Environmental Protection Agency's Energy Star Program, the Department of Energy's Rebuild America initiative and Hospitals for a Healthy Environment.

40%

Energy demand
Buildings consume 40% of global energy

Zero

Energy consumption
We envision a world where buildings are energy self-sufficient

Reaching out to schools

Most would agree that school budgets should go toward books – not to unnecessary electricity bills to run old, inefficient lighting. Lower quality lighting that leaves many children squinting. That's why we're reaching out to schools. Plus, we have the opportunity to teach children about living a more environmentally responsible lifestyle.

Sharpened focus

In keeping with our targeted approach to social investment activities that reflect our business, we are directing our efforts toward projects to upgrade lighting, particularly in schools.

One initiative is our Global School Program on Energy Efficient Lighting that raised awareness among students in five schools around the world – in Brazil, China, Germany, South Africa and the US in 2007. Each school was given a grant to upgrade its lighting and the students became lighting designers.

They were trained and asked to define their present lighting infrastructure both in terms of cost and CO_2 emissions, using tools we provide. The program also allowed the students to learn from one another via teleconferences, connecting with children on the other side of the globe. Students in Germany talked to their counterparts in China and the US during separate calls.

Inspiring students in Hong Kong

In Hong Kong we've called upon students to adopt a more environmentally friendly lifestyle by making a "simple switch" to more energy-efficient lighting. At year end, more than 110 schools with more than 20,000 students at the primary, secondary and university levels had enrolled.

"Energy saving and environmental protection are major policy areas of the Hong Kong Special Administrative Region Government," explains Wiebo Vaartjes, CEO of Philips Hong Kong. "We are echoing this by educating the 'future pillars of society' to be socially responsible."

Teaching preschoolers

Amid the excitement of graduating from Tadika Philips Batu Arang, our kindergarten in Malaysia, 25 preschool children received an extra life lesson. They learned how to save energy on their special day, organized during the country's Energy Month in November 2007.

The Philips CeTree (Center of Education, Training on Renewable Energy and Energy Efficiency) Mobile Energy Efficient Show Home paid them a visit. The youngsters gained hands-on experience thanks to the Show Home's five knowledge kiosks – General Knowledge on Renewable Energy, Energy Efficient Electrical Equipment, Solar Thermal, Solar Electric and Biomass. CeTree personnel also talked to them about the importance of energy-saving habits.

Green light means safe flight

Every year some 60 million birds migrate across the North Sea. Most make the trip across without any problems. But under certain weather conditions many are attracted by traditional lighting on oil and gas platforms and they become disoriented.

They fly around aimlessly or land on the platforms. This delay proves fatal because migratory birds have very limited reserves. By the time they continue their migration, some of them are too weak to reach land safely.

The risk of the birds encountering such specific weather conditions en route is about 10% – that's 6 million birds.

Color is key

NAM (a joint venture between Shell and Exxon) spent many years studying this and involved Philips. Their work showed that the key to solving the problem lies mainly in the color of the lighting used on the offshore platforms.

Birds are distracted predominantly by the red part of the spectrum, and much less by blue or green. Blue lighting, however, would mean less safe conditions for the people working on the platforms, partly because that kind of light impairs the sharpness of one's sight. Fire extinguishers are also less clearly visible in lighting without the red part of the spectrum.

So NAM and Philips jointly set about developing a new type of light that would not distract birds, while not impairing safe working conditions. The result is a new type of lighting that radiates only a limited part of the color spectrum.

Promising results

This new lighting has been installed as a pilot project on a NAM platform off the island of Vlieland along the Dutch coast – with very promising results. During the trial period the number of distracted birds was counted and the welfare of the people working on the platform was also studied. The trial was carried out in accordance with regulations for safe, healthy working conditions.

The first scientific results became available after the main bird migration season in the autumn. Compared to observations made in previous years, the number of attracted birds was reduced up to 10 times. Some of the "white" lighting was not yet replaced. The expectation of the biologist who did these observations is that a full replacement could eliminate 90% of the attraction. And a number of other oil companies have shown interest in this new lighting.

Green

The right light
Green lighting means safety for migratory birds

A range of options

The time is now
Today's energy saving lighting solutions meet the needs of customers and the planet

Energy saving solutions

Since 1980 when we invented the energy saving compact fluorescent light bulb, we have worked hard to make improvements and develop new solutions. Many options are available today with more exciting possibilities to come. Each offers significant savings in energy use and CO_2 emissions, as shown above, as well as cost savings. This is just a sample of the products we offer to address a wide range of applications and customer preferences.

For each market segment an energy efficient lighting solution is already available

Lighting area	Old technology		Today's energy savers	Energy savings	CO_2 savings per lamp per year
Road lighting	High pressure mercury lamp	▶	**CosmoPolis**	**58%**	**133 kg**
Shop lighting	Halo	▶	**Ceramic discharge metal halide**	**86%**	**140 kg**
Office and industrial lighting	TL8	▶	**TL5**	**61%**	**94 kg**
Home lighting	Incandescent	▶	**CFLi**	**80%**	**42 kg**
Home lighting	Incandescent	▶	**Halogená Energy Saver**	**30%**	**16 kg**
LEDs	Incandescent	▶	**LED**	**80%**	**40 kg**

"LEDs run cool, so unlike traditional incandescent bulbs they don't waste energy producing unwanted heat."

The future of lighting

Investing in the future

We continued to invest in our Lighting business in 2007. The EUR 1.8 billion acquisition of Genlyte leverages our earlier successful acquisitions of Color Kinetics, Partners in Lighting, TIR and Lumileds.

Lighting goes solid state

Light-emitting diodes (LEDs), those small solid-state lamps that were once only good for showing that your video recorder was on, are fuelling a major revolution in the lighting industry. The reason is that LEDs have gotten brighter. Their luminous efficacy – the amount of light you get out compared to the electrical energy you put in – already surpasses that of tungsten and halogen lamps. Soon it will even exceed that of fluorescent lamps.

LEDs have always had some advantages over other types of lamp. They are small and rugged, have no glass to shatter and offer typical lifetimes in excess of 50,000 hours. They can be made in a range of spectrally pure colors, or laced with suitable phosphors to emit broad-spectrum white light.

Peter Wierenga, CEO of Philips Research, explains: "LEDs run cool, so unlike traditional incandescent bulbs they don't waste energy producing unwanted heat. They're efficient and long lasting – a typical LED will work for more than 11 years if used 12 hours a day."

The downside is their cost. Like other new technologies that hit the market, LEDs are expensive. The cost of LEDs today could be compared to the price of a compact fluorescent (CFLs) in 1985. But with lower energy consumption, LEDs lower energy bills. And as economies of scale take hold, costs will decrease.

As inherently digital devices, LEDs produce light that can be intelligently controlled to dynamically customize environments, from restaurants and casinos to retail shops, city beautification projects and offices. Currently used primarily in specialty applications where CFLs are not suitable LEDs hold great promise for the future of general lighting.

The future of indoor lighting

Imagine ceilings literally glowing with color, glass walls that light up at the flick of a switch, windows that provide subtle illumination after dark. Interior lighting is set to change.

No more glaring bulbs or flickering fluorescent lamps. Instead, large areas of evenly distributed light that can be adjusted in brightness and color and can be applied to almost any surface in almost any shape. This is the exciting world of organic light-emitting diodes (or OLEDs, for short).

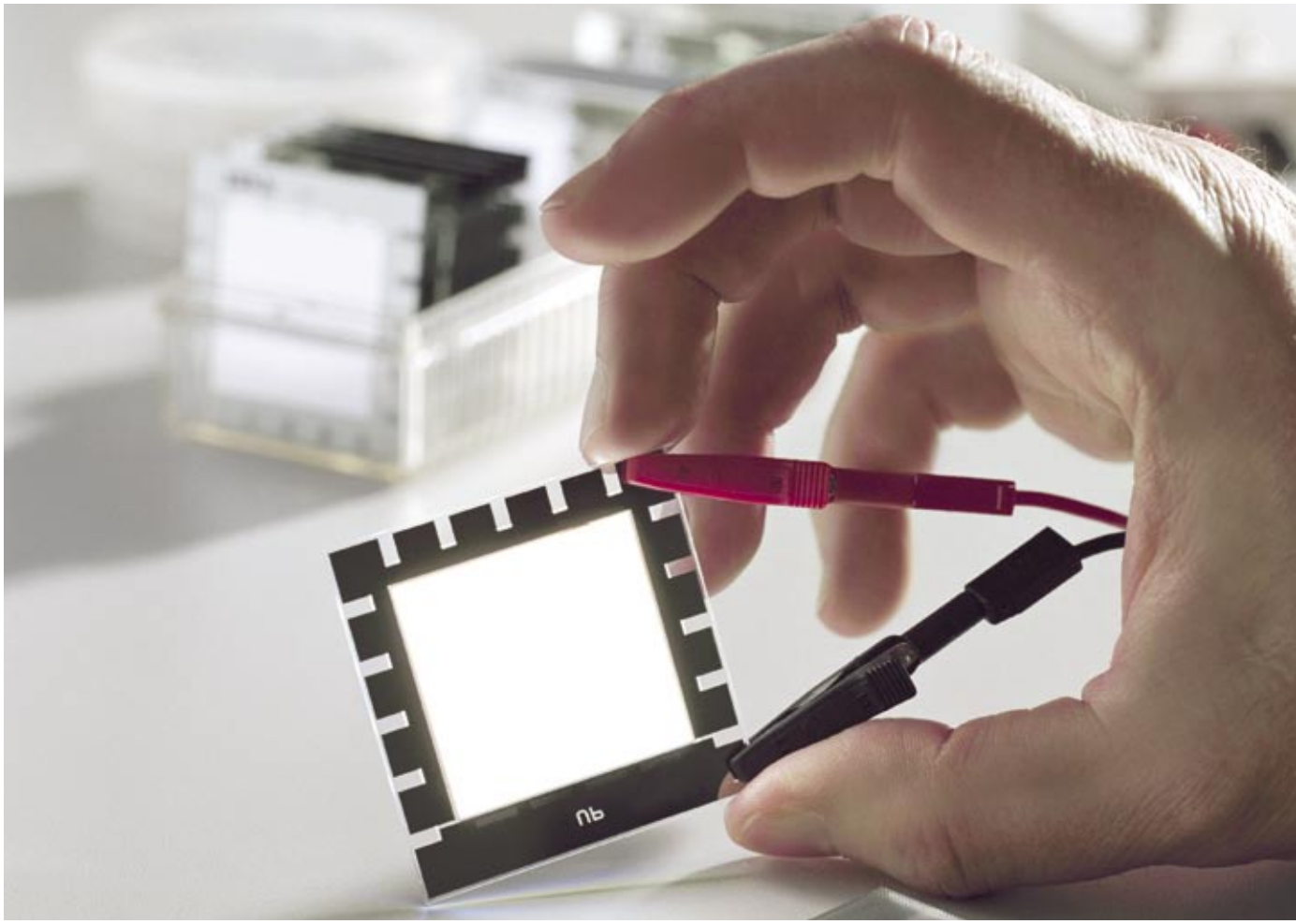
Scientists at Philips Research have been working to develop OLEDs as a new light source for homes,

Long life

Energy efficient
LEDs can last more than 11 years if used 12 hours a day

€1.8 billion

Acquisition
Acquiring Genlyte strengthens our position in LED solutions



Philips prototypes of colored organic LEDs (Light-Emitting Diodes) for lighting applications.

workplaces, stores, public areas, and even cars and planes. OLEDs will not only enhance the look and feel of interior spaces, but – like LEDs – will be better for the environment.

Since OLED light is not yet powerful enough to provide full illumination, it will initially be used for decorative purposes. However, the range of applications will expand dramatically as the technology develops. The size of panels is also set to grow: current prototypes are 5cm x 5cm up to 15cm x 15cm, but panels of 60cm x 60cm are envisioned. We have developed plain white and "warm white" panels, while "color-variable" OLEDs – capable of producing light of almost any color (including mimicking daylight and traditional lighting) – are likely to appear in the next 3-5 years.

Consumer Lifestyle: Offering responsible choices

We know that consumers are seeking better wellbeing for themselves and those closest to them. And, increasingly, they are also seeking better wellbeing for society as a whole, and the environment in particular.

With our longstanding commitment to reduce the environmental impact of our products, we enable consumers to make simple, responsible choices about the products they buy and the impact they have before, during and at the end of their life cycle.

Addressing power consumption

We have made several advances in addressing power consumption, for example with greater use of innovations in our FlatTVs like dimming backlights, ambient light sensors and image processing intelligence that calculates where energy consumption can be reduced for every image displayed. Of course our focus isn't limited to television. Across our product range, we are uncompromisingly driving sustainability in all aspects of product creation through our EcoDesign process.

From simple innovations like packaging and easier disassembly for recycling, to rechargeable batteries which last 20% longer without charging, we are offering consumers more sustainable choices.

Plus, we will help make those choices easier when consumers shop thanks to the Philips Green logo, which will clearly identify products that have a significantly better environmental performance than their competitors or predecessors.

Sustainable innovations

Our efforts to make a positive environmental contribution have not come about overnight. With our new Consumer Lifestyle sector we have brought together considerable competency, knowledge and expertise of the sustainability teams from our former Consumer Electronics and Domestic Appliances and Personal Care businesses. Innovation projects are running and the sector has conducted workshops with Research to determine long-term opportunities.

Green Products

Here are some of our Green Products that allow consumers to save on their energy bill and contribute to reducing the effects of climate change.

EcoDesign

Driving environmental improvement
Our EcoDesign process focuses on creating products that offer better environmental performance

73%

Less energy
Our Cineos SoundBar DVD Home Theater uses 73% less energy than the average of its competitors

Breakthrough

Standby power
The Philips Sonicare FlexCare offers best-in-class standby energy consumption

The Philips Cineos SoundBar DVD Home Theater HTS8100 uses 73% less energy than the average of its competitors. This home theater won a Bronze Hong Kong Eco-Products Award 2007.

The Philips widescreen flat TV 32PFL5522D/12 32-inch LCD integrated digital with Pixel Plus HD uses 15% less energy than the average of its competitors.

The Philips Digital Audio Video Player SA5125 uses 15% less energy than the average of its competitors. It earned a Silver Hong Kong Eco-Products Award 2007.

The Philips Sonicare FlexCare offers a breakthrough in standby energy consumption – a best-in-class low of 0.5 watts, down from approximately 1.6 watts, compared to its competitors. And the charger automatically shuts off when the toothbrush is fully recharged. The result: up to 66% less energy consumption per year.

A shared commitment
Our retail partners are looking for us to team up with them, just as we look to our suppliers to team up with us to meet consumers' needs.

Retailers and consumers are increasingly interested in what we're doing to reduce the environmental impact of our products, especially in terms of improving energy efficiency.

We believe that this is an integral tool to go to market with. Wal-Mart, one of our biggest customers, agrees.

Wal-Mart's own environmental goals are ambitious: to be supplied 100% by renewable energy, to create zero waste and to sell products that sustain our resources and environment.

"Philips is a leader in promoting sustainable products and marketing solutions that are a win-win for our company and our customers worldwide," said Paul Lewellen, Senior Director of Supplier Development for Wal-Mart International.

"Whether it's working to drive sales of energy-saving light bulbs in Argentina, or encouraging customers to donate old television sets to charity through an innovative trade-in promotion in Brazil, it is clear Philips shares Wal-Mart's strong commitment to sustainability throughout the global retail supply chain."

Energy efficient solutions for emerging markets

Less wood, less emissions and more time

We completed the commercial pilot for the Philips Woodstove – a smokeless, fuel-efficient stove – which ran between 2006 and 2007 in the Indian states of Maharashtra, Tamil Nadu and Uttar Pradesh.

We gained knowledge in many areas, including production, distribution, financing models and the role of non-governmental organizations. We also learned more about our consumer. For example, 60% of the households have two incomes and their occupations include farming, tailoring, working in a factory or for the government, driving a truck or owning a shop. People who cook with wood bought our woodstove, along with people who use other fuels like kerosene or gas. And most households have multiple stoves used for specific tasks like boiling bath water or making tea and bread.

Improved quality of life

Our innovative Woodstove dramatically reduces smoke emissions and indoor air pollution. Women and small children, who traditionally do the cooking, breathe in the equivalent of two packs of cigarettes a day.

Yet the main perceived benefit for consumers is not health-related. Rather it is about lifestyle improvement – fast and clean cooking with less wood and the added benefit of less CO_2 emissions.

Faster clean-up

According to one user, "I like that it cooks so fast. Since we have the Philips Woodstove making breakfast and cleaning up is much faster than before so I can leave earlier for work and spend more time working."

We also learned that some of the wood used in India contains certain substances that can affect the lifetime of the stove's burning chamber, so we are currently testing new materials and expect results in early 2008.

Fuel efficient

Less wood
Our Woodstove saves up to 50% of the wood used with a traditional stove

1.6 billion

Living without light
Lighting is a basic need for the 1.6 billion people who lack access to electricity

Sustainable lighting

Our SMILE (Sustainable Model in Lighting Everywhere) pilot was completed in 2007. Launched in 2006 in four Indian states, the pilot tested the product specifications of two lighting solutions: UDAY, a rechargeable portable lantern, and KIRAN, a hand-cranked LED flashlight. We also worked on establishing viable business models.

Getting confirmation

Clearly there is a need for innovative lighting solutions for people lacking access to the electricity grid and for those who have access that is unreliable. The pilot also revealed how price sensitive this market is and how important it is to provide affordable solutions.

The pilot confirmed how truly complex it is to do business at the base of the pyramid and how necessary it is to have hybrid business models rather than going for a single approach.

Expansion in India and beyond

Making use of this learning, SMILE products are now distributed in eight Indian states through a combination of channels. Depending on the state, distribution can be via kiosks, through our partnerships with microfinance institutions (MFIs) and non-governmental organizations (NGOs), or with rural/semi-urban channels.

Plans call for continuing expansion in India and refining our partnership strategies with NGOs, Self Help Groups and MFIs.

We are also extending SMILE to Africa, where the product portfolio includes a solar-charged battery-operated lantern. New developments are also underway with solid-state-enabled lighting in order to create breakthroughs in price, energy efficiency and added functionalities.

I feel better now

Philips and healthcare

"Until the doctors could find out what was wrong with me, I was really scared. I tried to be brave but it was really hard. Then my Mom and my best friend went with me to a different hospital. The doctors let us put my favorite toy in a 'kitten scanner' for an exam. Because I'm a big girl, I can use the regular 'cat scanner.' And I was just as brave as my toy!"

Philips Ambient Experience can help to reduce anxiety by inviting patients to do their own scans on the "kitten scanner" before they go in for their own exam.

Changes and challenges

Everywhere we look, we see contradictions. Between the aspirations of patients and the funding necessary to make them a reality. Between the brilliance of scientific breakthroughs and their universal availability. Between those who can afford the very best that healthcare can offer and those who have no access and can afford nothing. Between the ease of delivery in large cities and the seemingly insurmountable challenges of reaching out to far-distant rural regions.

Everyone working in healthcare does so under the growing reality and burden of demographic and epidemiological change, rising costs and medical and scientific advances.

Demographic demands

Healthcare costs have been rising inexorably in developed and developing countries, and there is no sign that this trend can be reversed. The numbers tell the story.

The predicted world population for the year 2020 is 7.5 billion and is on track to surpass 9 billion by 2050, according to the latest official United Nations population estimates and projections. If so, spending on healthcare in 2050 would equate to EUR 8 trillion – if growth rates remain stable from 2020.

Right now, the global population is not only growing, it's also getting older, which puts greater pressure on the world's healthcare providers. Since 1950 the proportion of older persons (those aged 60 or older) has been rising steadily, moving from 8% in 1950 to 11% in 2007, and is expected to reach 22% in 2050. That's 2 billion people.

A global issue

This is not just a problem for developed countries. While population aging may be less advanced in developing countries, the UN reports that the populations of a majority of them are set to enter a period of rapid population aging.

Older and sicker populations will push up healthcare costs in China, India and elsewhere dramatically over the coming years. In developing countries as a whole, just 8% of the population is today aged 60 years or over but by 2050, 20% of their population is expected to be in that age range.

And what's more, as populations in emerging economies adopt western lifestyles and diets, chronic diseases will begin to affect and claim more lives. In fact, this is already happening.

The rise of chronic diseases

According to the World Health Organization (WHO), chronic diseases, such as heart disease, stroke, cancer, chronic respiratory diseases and diabetes, are by far the leading cause of mortality in the world, representing 60% of all deaths. WHO says this "invisible epidemic is an under-appreciated cause of poverty that hinders the economic development of many countries. Contrary to common perception, 80% of chronic disease deaths occur in low and middle income countries." This is both a human tragedy and a financial burden, as the management of chronic diseases is very expensive.

The Institute for Healthcare Improvement, a non-profit organization based in Cambridge, Massachusetts, US, forecasts that such trends mean "many healthcare systems around the world will become unsustainable by 2015."

We know what's happening to populations and the resulting impact on healthcare costs. We see changes in diseases patterns as chronic conditions become manageable and more pervasive worldwide. We can also be certain that medical researchers will continue to roll back the frontiers of knowledge and practice in technology, pharmacology, equipment and procedures, creating new opportunities to prevent, cure and decelerate disease.

The truth of the matter

It is easy to be overwhelmed by the complexity of such a scenario. But then it is ever more important to state simple truths.

And here it is: we must deliver better quality care at lower cost – all as efficiently as possible.

9 billion

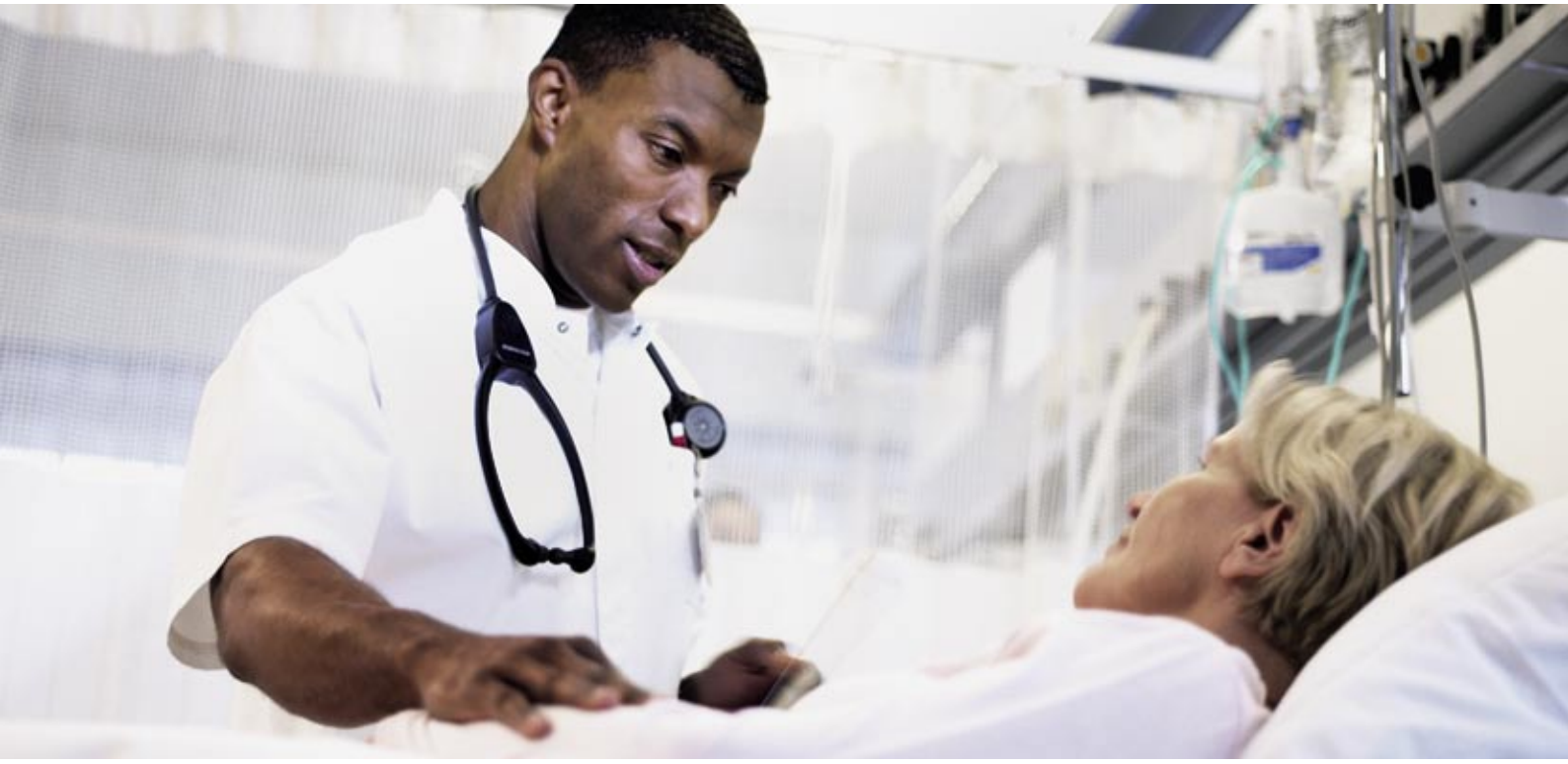
Population growth
World population is likely to surpass 9 billion by 2050

60+

Unprecedented aging
By 2050 there will be 2 billion people aged 60 or older

€8 trillion

Projected spending
Global healthcare costs will increase with the population

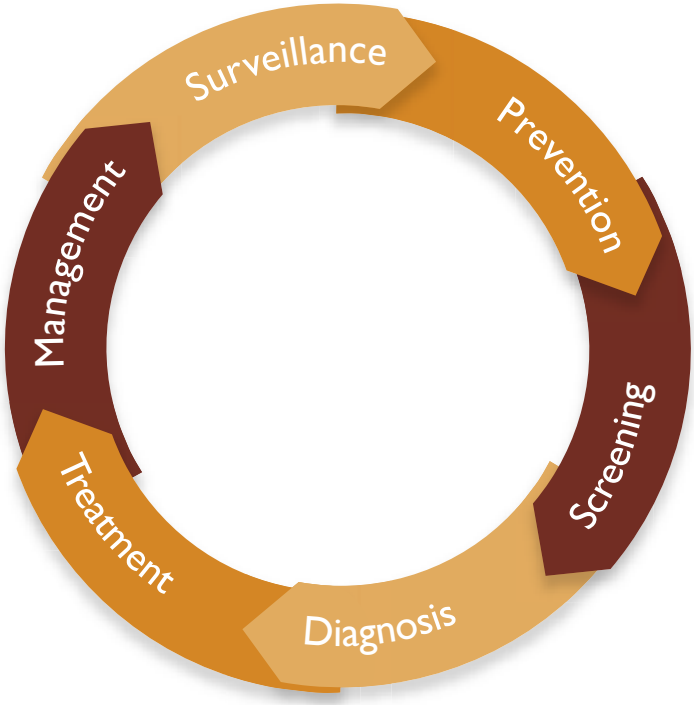


What we believe

As a global business we are acutely aware of our duties as a citizen of the world and the role we can play in improving people's lives.

We believe concerted action in healthcare is a social responsibility. Realizing real and immediate differences in the way the world thinks and acts in healthcare is our passion. We believe healthcare is a fundamental right to which every human is entitled.

At Philips we advance healthcare by making a difference to people. Partnering with the broader healthcare community, we seek to facilitate new solutions for change to drive better health outcomes.



Putting people front and center

At Philips we are proud to be at the cutting edge of medical technological advancement. But technical expertise isn't the only thing a healthcare company needs to make a difference – each new innovation we develop should also be useful and meaningful. To do that, we focus on the people at the center of healthcare – the patient and the care provider. Globally we deliver innovative healthcare solutions designed to address the needs of patients as well as healthcare professionals.

#1

Global killer
More people die from cardiovascular diseases than from any other cause

We listen

Seeking insight
We focus on the needs of our customers and the people they take care of

Our focus is to bring innovations that will reduce the incidence and severity of many of today's deadly and debilitating diseases with a particular focus on the fields of cardiology, oncology, critical care and women's healthcare. Whether it is in the hospital or in the home, we seek to improve patient outcomes throughout the entire course of care – from prevention and screening to diagnosis, treatment, management and surveillance. It's about looking beyond the traditional areas of diagnosis and treatment.

"Both patients and caregivers struggle with a complex, fragmented healthcare system," explains Steve Rusckowski, CEO, Philips Healthcare. "We believe the best way to reduce this complexity is by addressing the needs of the healthcare industry from the perspective of patients and their health problems."

We listen to the people who use our products, our customers and their patients. And at the same time, we examine every aspect of the disease management process, from home to hospital. This human insight combined with a solid clinical understanding enables us to create integrated offerings across the cycle of care.

One holistic process

"To provide better, more cost efficient healthcare we focus on our customers and the people they take care of – the patients. This sets us apart," says Rusckowski. "We view every single aspect of each patient's treatment, from the initial diagnosis, to testing, monitoring and aftercare, as part of one holistic process: the care cycle. That's why Philips provides healthcare solutions for the home as well as for hospitals, including personal alarms, home defibrillators and devices that monitor chronic diseases, like congestive heart failure."

Indeed, this way of working supports clinical excellence. "This approach doesn't just let us put our customers and patients first, it also allows clinicians and care providers to spend more time doing what they do best – treating and managing their patients' conditions. We want to help build high quality, patient-centered healthcare systems. And to do this, we need to provide integrated, innovative solutions for every stage of the care cycle," Rusckowski says.

Steve Rusckowski, CEO, Philips Healthcare

In the following pages, you will see how we are doing just that in the field of cardiology. Through our approach we can really make a difference in the worldwide cardiovascular disease (CVD) burden. The number one cause of death globally, CVD is projected to remain the leading cause of death and is a major cause of disability. The World Health Organization believes that if appropriate action is not taken by 2015, an estimated 20 million people will die from cardiovascular disease every year, mainly from heart attacks and stroke.

A global burden

Cardiovascular disease

Caused by disorders of the heart (cardio) and blood vessels (vascular), cardiovascular disease includes heart attacks, stroke, raised blood pressure, peripheral artery disease, rheumatic heart disease, congenital heart disease and heart failure. Once associated only with overweight, overworked middle-aged men, heart disease has no boundaries. It affects men, women and children in all socio-economic groups, everywhere in the world.

World Health Organization (WHO) statistics reveal that at least 20 million people survive heart attacks and stroke every year. A significant proportion of them require costly clinical care, which puts a huge burden on long-term care resources. CVD affects people in their mid-life years, undermining the socioeconomic development, not only of affected individuals, but families and nations.

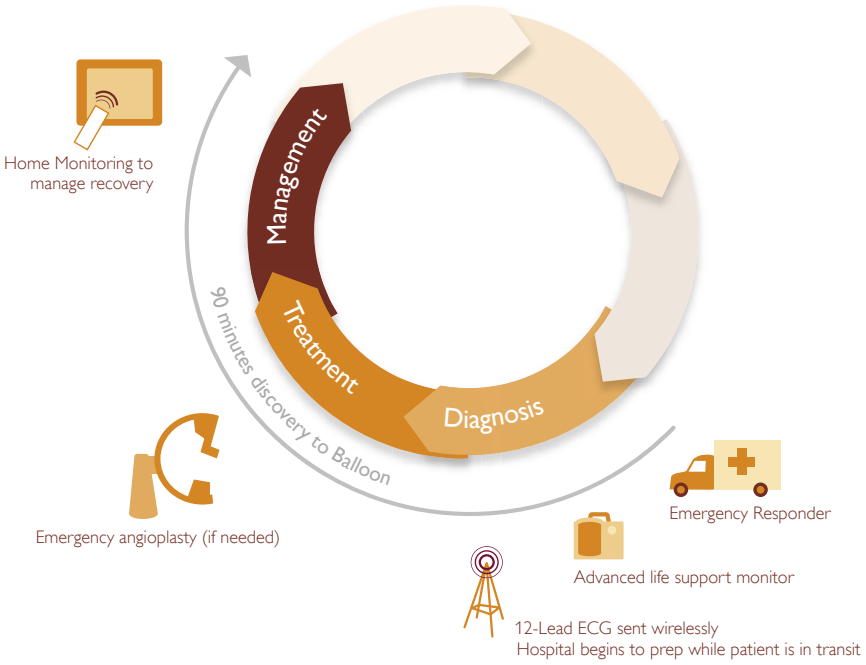
High costs

The costs are high in human and financial terms. A few examples: According to the American Heart Association the estimated cost of cardiovascular disease for 2007 in the United States is nearly EUR 300 billion, including health care services, medications and lost productivity. Overall CVD is estimated to cost the European Union economy some EUR 240 billion a year. WHO estimates that between 2006 and 2015, China will lose EUR 380 billion in foregone national income due to the combination of heart disease, stroke and diabetes.

"We simply cannot afford to focus only on extremely costly and traumatic surgical interventions. We have to concentrate on prevention, early diagnostics and remote patient management," says Gerard Kleisterlee. "Our goal is centered on our customer's goal – the delivery of better, more efficient care through earlier diagnosis, fewer disabilities, faster recoveries, and in cases of long-term care, slower progression of disease."

16.7 million

Lives lost
Cardiovascular disease causes nearly 30% of total global deaths



Speeding time and treatment

Our focus on the cycle of care – An example

Every minute counts for a heart attack victim. As soon as a heart attack occurs, the heart muscle starts to die. That's why reducing the time between heart attack and treatment has been proven to have a big impact on a patient's long-term recovery.

"As a result, the American College of Cardiology, in partnership with the American Heart Association and other organizations around the world, has launched the 'Door to Balloon' campaign. It aims to reduce the amount of time from the arrival of the patient at the hospital to angioplasty – known as balloon – to 90 minutes or less," explains Joris van den Hurk, Vice President of Cardiology Care Cycles for Philips Healthcare.

This goal addresses the single most critical challenge tied to treatment at the onset of cardiac arrest – length of time elapsing before the blocked artery is reopened. With speed the goal, it is critical that emergency responders shorten the time from arrival at the emergency department to the time of treatment.

Philips HeartStart MRx Monitor/Defibrillator enables the "Door to Balloon" process to begin before the patient gets to the hospital. With the MRx a paramedic can transmit a patient's electrocardiogram (ECG) data from the ambulance to a hospital's emergency department. Clinicians can use the ECG to begin assessing what treatment the incoming patient will need.

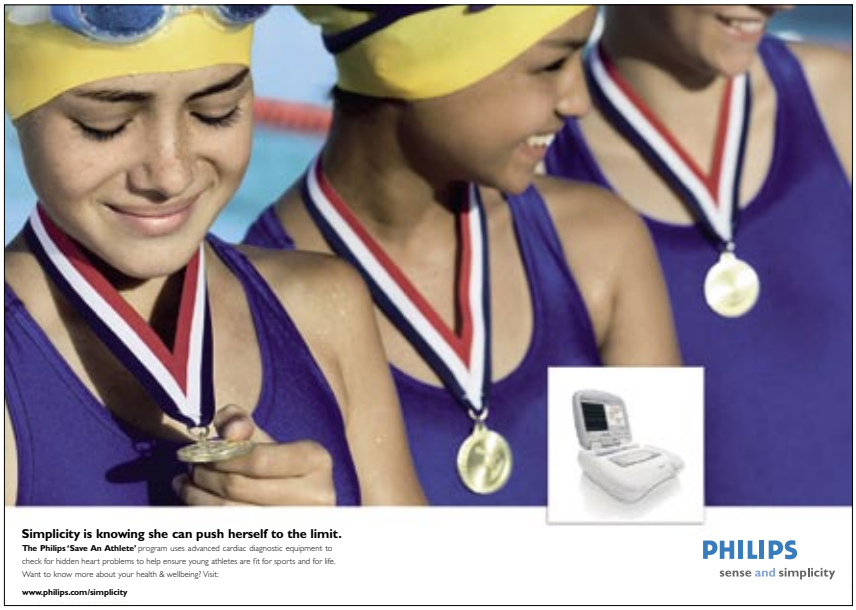
Since the MRx allows a hospital to begin organizing its resources – before a patient even arrives – it can dramatically reduce the delay to treatment. Another benefit is the ability to potentially divert the patient to a specialized hospital. Patients can bypass the emergency department and go directly to the cardiac catheterization lab for angioplasty. This, too, can clearly speed time to treatment.

In the "Door to Balloon" protocol, the clock starts when a patient is brought into the hospital. The MRx allows hospitals and EMS to start the clock earlier, offering a "Discovery to Balloon" solution. All the prep, scheduling, diagnostic and routing activities – which usually start once the patient arrives – can now begin while the patient is en route, saving valuable time.

After hospital treatment, the patient can be remotely monitored in their home with our telehealth solutions detailed on pages 62-63.

Raising awareness

A key ingredient in preventing cardiovascular disease is raising awareness – alerting people to the fact that heart disease poses the greatest health risk and is more likely to kill than any other disease. Research shows that those who recognize this are more likely to take action to protect themselves and their families.



Simple tests for student athletes

Our Save an Athlete program aims to improve health and wellness by educating student athletes, their families, doctors, athletic directors and coaches about preventing sudden death through early cardiac testing. Launched in 2006 in the US, the program offers free screening of student athletes for potentially lethal heart conditions using ultrasound technology.

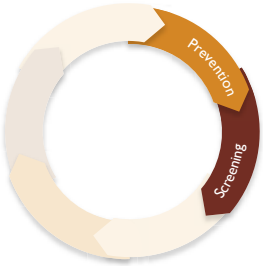
"The use of cardiac testing with ECG and echo exams in sports physicals can help identify heart conditions that could trigger sudden death that would not be otherwise identified through an ordinary examination or medical history," says William Rappoport, M.D., F.A.C.C., Arizona Heart Institute.

During the second quarter of 2007 we launched a branding campaign showcasing a range of solutions that empower consumers to manage their health and wellbeing. One of the advertisements focused on Save an Athlete, which has been extended to the UK.

Your Mouth, Your Heart

The Philips Sonicare website educates consumers about the strong link between oral health and overall health, and heart health in particular.

Recent studies have revealed that people with periodontal disease very often have heart disease as well. Researchers believe that this is due to oral bacteria present in gum disease, which can affect the heart if they enter the bloodstream. It has been shown that these bacteria can attach to fatty deposits in the coronary arteries and



€35 million

The Philips-led MyHeart consortium
One of the largest biomedical research projects in the EU, MyHeart is focused on preventing and managing heart disease

contribute to arterial clot formation. Such clots can dislodge and are responsible for heart attacks and stroke.

While periodontal disease doesn't necessarily cause heart disease, it is nevertheless a good risk indicator. Fortunately, elimination of the gum infection by thorough professional care can eliminate the bulk of those bacteria and may actually lower the risk to the heart. Excellent plaque control through good oral hygiene will decrease the risk of re-infection and ultimately may help improve overall health.

www.sonicare.com

Educating people in Eastern Taiwan

The largely mountainous and densely forested terrain in Eastern Taiwan makes its populated areas difficult to reach. As a result, the standard of living there is generally lower. People are often poorly educated and less aware of health issues. To help change that, in 2005 we launched a four-year educational campaign with the theme "We care for your health."

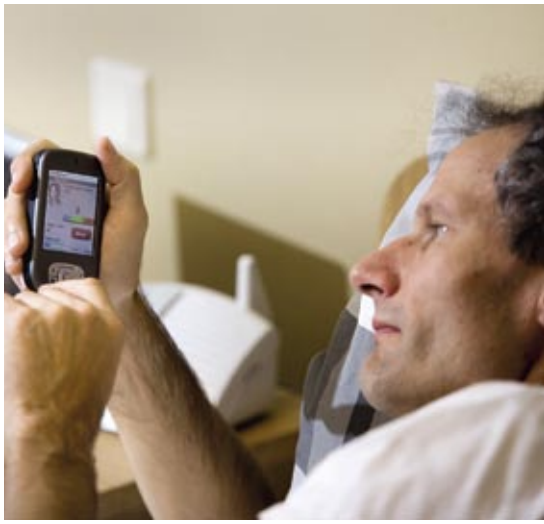
Called Naruwan – translated "How are you?" in aboriginal Taiwanese – this program focuses on improving oral health. In 2007 we worked with the Hua-Lien County Health Bureau, conducting 16 seminars on preventing gum disease attended by more than 700 people. We also supported the Tai Tung Health Bureau in training 85 school nurses on how to teach children about oral health.

Early detection

The Philips-led MyHeart consortium has identified four key product concepts that are likely to bring the most benefit to the prevention and management of chronic cardiovascular disease:

- Activity Coach – to maximize the enjoyment and health benefits of regular exercise, targeted primarily at healthy individuals.
- Take Care – to assess and reduce risk factors for cardiovascular disease through vital body sign monitoring, lifestyle coaching and motivation, targeted at those who are at risk of developing cardiovascular disease.
- Neuro Rehab – to improve and shorten the rehabilitation period through physical and mental exercises, targeted primarily at heart attack and stroke victims.
- Heart Failure Management – to improve quality of life and life expectancy for heart failure patients through early detection of deterioration in their condition and improved patient management.

The principal technology development common to all of these applications are body sensors and wearable electronics that can unobtrusively detect and measure vital body signs, communicate and analyze



the acquired data and provide feedback to users or health providers.

Prototype disease management systems for heart failure patients will enter clinical evaluation in 2008 in Germany and Spain. This will include an electronic weight scale and blood pressure monitor, a zip-up body vest with integrated electrodes and control electronics to measure the patients electro-cardiogram, and sensors placed in the patient's normal bed to measure heart- and breathing-rate, and body movement while sleeping.

The MyHeart project, one of the largest biomedical and healthcare research projects within the European Union, has a budget of about EUR 35 million, of which EUR 16 million is funded by the European Union. The consortium comprises 33 industrial, research, academic and medical organizations from 10 European countries.

Earlier diagnosis

At Philips we believe that the world simply cannot afford to focus only on extremely costly and often traumatic surgical interventions. We also look at prevention, early diagnostics and remote patient management. This is essential to better patient outcomes.

Better in many ways

"Stunning three-dimensional images of the inner workings of the body."

That's how media reports describe our new 256-slice Brilliance iCT scanner, which has been specifically designed to make the job of the clinician easier and improve the experience of the patient. How? By allowing radiologists to produce high-quality images with exceptional speed, including complete coverage of the heart and brain, and can also show changes over time. It's so powerful it can capture an image of the entire heart in just two beats, while incorporating Philips technology that has reduced radiation doses by up to 80%.

Our DoseWise Radiation Safety program includes techniques, programs and practices that ensure optimal image quality, while protecting people in X-ray environments. This is an important parameter we consider at every level of new product design and development. Therefore we have expanded the definition of our Green Focal Area on hazardous substances to include this topic.

Education for dose reduction methods is delivered through operator documentation, on-site application training, off-site training and specific publications.

Strengthening our position in emerging markets

In line with the strategy to bolster our healthcare presence in emerging markets, we acquired Brazil's leading general X-ray manufacturer, VMI-Sistemas Medicos, expanding our local position in the Latin American market. With the ability to produce X-ray equipment in Brazil we will be able to offer more affordable solutions to the local market. And the impact of this acquisition goes beyond Brazil as we plan to boost VMI's Brazilian exports to other countries in Latin America.

We also entered a number of strategic agreements, including a contract with Ascent Profit, a Chinese medical equipment wholesaler, to deliver high-end radiography systems in China.

€250 million

Professional Healthcare Solutions turnover
We have implemented projects in Ghana, India, Indonesia, Jordan, Kenya, Morocco, Tanzania and Uganda

Access

Bringing healthcare to remote areas
Our innovations make healthcare available to people who were beyond the reach of centralized facilities

Connecting cardiac centers

Patients in rural areas of the Philippines are benefiting from the advanced medical treatment available for degenerative diseases of the heart, lungs and kidney thanks to Philips and our partners who participated in a seven-year project partially funded by the Dutch government and the Philippines Department of Health.

Our EasyWeb Healthcare System connects three satellite hospitals to the Philippines Heart Center in Manila. This Internet-based system allows online referral and diagnosis of patients from remote provinces by healthcare experts in Manila. Now health screening and healthcare access are available to thousands of people outside Metro Manila who were previously beyond the reach of the modern healthcare system. Because clinical images, along with voice and real-time images of the doctor and patients can be transmitted quickly, diagnosis and a plan of action for therapy can be agreed upon faster.

Making quality services available

Dr. Criselda Abesamis, Director of the Philippines National Center for Health Facilities Development, says: "The project is to make sure that the quality of health services that are centralized in Metro Manila are now decentralized and available in the rest of the Philippines."

This EasyWeb system will help the Philippines Heart Center and the regional hospitals to be more productive and efficient. The system also offers research and education applications for physicians as patient studies can be shared across hospitals.

Plus, specialists can now work with the same quality of medical equipment as their counterparts in the West, which makes is much more attractive for them to remain and work in the Philippines. Dr. Abesamis says the project is a "strategic solution to solve the outward migration of our specialists."

Professional Healthcare Solutions

Projects like the work at the Philippines Heart Center are managed by Professional Healthcare Solutions, a dedicated group within our Multi Country Region Sales and Service organization. This group focuses on healthcare projects for emerging markets.

The team has unique experience in combining our Healthcare products and service portfolio with financing solutions and value-added services such as consultancy, facility services, training and education. Integral hospital solutions are offered in cooperation with partners for construction and installation.

Since 1993 we have carried out healthcare projects in developing countries representing a turnover of more than EUR 250 million. We have implemented large-scale projects in Ghana, India, Indonesia, Jordan, Kenya, Morocco, Tanzania and Uganda, and are currently working in China, the Philippines, Uganda and Zambia.

Changing diagnostics

Medicine as it is practiced today focuses on how the human body functions at the level of individual organs like the heart, liver or lungs. This is addressed well with traditional imaging and patient monitoring solutions. But with advancements in the life sciences, such as the unraveling of the human genome, we now understand that diseases have their origin at the molecular level. Due, for example, to errors at the DNA or protein level. Our aim with next generation diagnostics is to detect these errors.

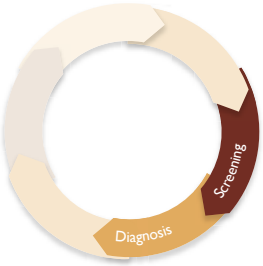
Diagnosing disease at the molecular level

Modern in vitro diagnostic tests are based upon the patient's DNA, proteins or other biomolecules. These tests are carried out on a sample of a patient's blood or other body fluids, such as urine or saliva, or a cervical or oral swab.

Molecular diagnostic tests can detect DNA. This allows clinicians to determine whether a person is at risk of getting a certain disease, detect the presence of foreign DNA in the bloodstream originating from bacteria or detect mutations in a person's DNA that may be associated with cancer.

Screening and diagnosis

With novel protein-based tests, it is possible to determine how a person's immune system reacts to disease. Or whether a person is at risk of getting a heart attack. Or suffers from a metabolic disorder.



DNA

Molecular medicine
Tests based upon a patient's DNA, proteins or other biomolecules can determine whether a person is at risk of getting a certain disease, like stroke or heart attack

Decentralized rapid diagnostic testing

Central lab testing		Testing@point-of-need
Short time to result	▶	Rapid therapy decisions
Compact and simple to use	▶	24/7 availability
Personalized therapy selection	▶	Reduced cost, improved outcomes

Early diagnosis of cardiovascular disease

Next generation in vitro diagnostic tests will radically change the field of cardiology. As illustrated above, tests will be performed not only in centralized laboratories but also at the patient's bedside – at the point-of-need.

In many cases, the equipment used in centralized laboratories and decentralized near-patient in vitro diagnostic testing will be connected via wired or wireless networks into sophisticated healthcare informatics systems to provide clinical decision support and data storage facilities.

Identifying disease

Once a patient is taken ill and enters the hospital, it's all about rapid diagnostics, identifying the cause of disease and then supporting the clinicians in deciding what treatment to apply.

A very important ultimate goal is to change that with early diagnosis. This will allow us to deal with diseases essentially before they lead to serious symptoms. Genetic risk assessment for stroke or a heart attack, or early detection of molecular disease markers for cardiovascular disease will be possible right in the doctor's office. A patient entering the emergency room can immediately be tested to decide whether he or she has suffered a heart attack, of to decide what type of stroke he or she has suffered.

Open Innovation

We think and act beyond our own boundaries. In a spirit of what is called Open Innovation, we choose best-in-class academic and industrial partners who have competencies and interests that complement our own – creating competitive advantage for each party.

Molecular Medicine

Philips is one of the major Dutch companies in a consortium that initiated the Center for Translational Molecular Medicine (CTMM), headquartered at the High Tech Campus in Eindhoven, the Netherlands. The CTMM is dedicated to the development of medical technologies that enable early and precise diagnosis, and design of new and "personalized" treatments for the main diseases causing mortality and diminished quality of life: cancer, cardiovascular diseases, infectious diseases and neurodegenerative diseases like Alzheimer's.

The CTMM is a public-private partnership that comprises a multidisciplinary group of parties – universities, academic medical centers, medical technology enterprises, and chemical and pharmaceutical companies. The Dutch government provides a substantial contribution.

Collaboration in Shanghai

In December 2007, Philips and the Institute of Health Sciences (IHS) established a joint research laboratory within the IHS in Shanghai, China. The IHS is part of the Shanghai Institutes for Biological Sciences and is also affiliated with the Shanghai Jiao Tong University School of Medicine.

The joint laboratory will conduct advanced research in the field of molecular medicine, with the ultimate aim of creating new solutions for the early diagnosis of disease and for monitoring the effectiveness of subsequent treatment.

Making treatment less traumatic

We believe it is critical to concentrate on prevention, early diagnostics and remote patient management, yet clearly there are times when treatment is necessary. The goal is to provide the best possible care.

Minimally invasive interventions

Under the increasing pressures to both lower healthcare costs and improve outcomes, minimally invasive methods are replacing traditional surgical procedures as quickly as the technology allows. Many treatments that would previously have needed open surgery can be carried out using endoscopes, catheters and needles. Such minimally invasive approaches reduce trauma, thus minimizing damage to healthy tissue and requiring less pain medication. This is better for the patient and shortens recovery times.

Many minimally invasive procedures can even be carried out in an outpatient setting and generally, these procedures are less costly for the hospital. Yet, there are challenges. During open surgery, surgeons can see where they are and what they are doing. For minimally invasive interventions, specialists need other information sources to view their actions. That's where imaging comes in.

Seeing and treating the heart

Cardiac catheterization laboratories have been leading the move to minimally invasive interventions for several years. Cardiologists diagnose and treat coronary artery disease using a catheter inserted into the groin and threaded through the arterial vessel tree to reach the heart. To guide the passage of the catheter they use fluoroscopy (live X-ray imaging), usually from a C-arm system that can be moved and angled to get images from any position.

An injected contrast agent, which is opaque to X-rays, reveals the structure of the vessel through which the catheter passes and pinpoints narrowed arteries or blockages that need treatment. Treatment may be in the form of a balloon angioplasty (compressing the plaque against the wall of the vessel), stenting (inserting a small wire tube) or rotablation ("drilling" through plaque).

Streamlining procedures for cardiac rhythm disorders

Electrophysiology (EP) is one of the fastest growing markets in cardiology. However, EP procedures are highly specialized and require specific equipment and facilities. The procedures, which deal with the heart's electrical conduction system, are often performed in surroundings not specifically designed for this purpose. Taking this into consideration, Philips developed an integrated solution, which provides EP specialists with a comfortable and efficient working environment – the EP cockpit.

A new workflow concept for electrophysiology labs, EP cockpit enables physicians to streamline procedures to treat cardiac rhythm disorders.

The first Philips ambient electrophysiology cockpit opened in Berlin's German Heart Institute. It is the first catheterization lab in the world to have the unique EP cockpit.

300 doctors

Training for rural doctors
With the Chinese Red Cross we are educating village doctors in Beijing, Shanghai and Guangzhou

Training healthcare workers in China

World Health Organization data show that health workers are inequitably distributed throughout the world, with severe imbalances between developed and developing countries. We believe health education is essential in making healthcare accessible to medically underserved communities.

In partnership with the Chinese Red Cross Foundation, we launched the Philips Rural Healthcare Program in 2006. This three-year initiative will educate 300 village doctors in Beijing, Shanghai and Guangzhou and includes sponsoring a train-the-trainer program for those who will work with the rural doctors.

Our Rural Healthcare Program will also establish 10 Philips clinics and hospitals. So far five rural clinics have been established. In 2007 we invited well-known doctors to go to the clinic we sponsored in Guizhou with Philips volunteers. We provided medicine and two days of free diagnosis to the local villagers.

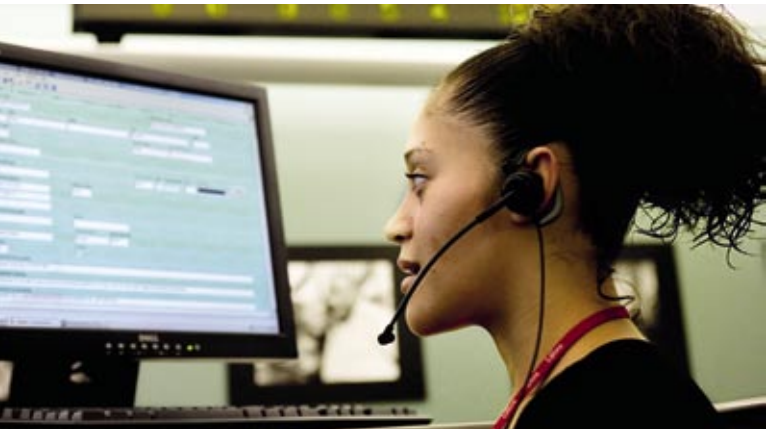
Personalized therapy

We are working on next generation tests that aim to eliminate the "trial and error" approach to medicine. Molecular tests can be used to select the appropriate drug therapy, based on genetic profiling, and to monitor therapy response. The key is that a patient will not receive a drug if it will not be effective. Plus, molecular tests can be used to monitor disease progression, or to maintain the appropriate level of drug taking.

At the Radiological Society of North America Annual Congress and Expo in November 2007, the research projects we showcased demonstrated where imaging technology for diagnosis and treatment planning for heart disease and cancer is heading. These included patient-specific organ models for personalized radiology planning, therapy and reporting. Also shown was a project dealing with new image analysis techniques to enhance the image resolution and quality of PET and SPECT scans and extract quantitative information relating to localized tissue processes, such as reduced oxygen levels in tissue.

Bringing remote care closer

Research consistently shows that elderly patients or those with chronic illness would much rather be at home than in an institutional setting. Home care is far less costly too. Plus, the increasingly aging population in many countries simply will not be able to be cared for in traditional facilities.



Philips has been active in telehealth for more than seven years, enabling disease management firms, home care agencies and healthcare providers to remotely monitor chronic disease patients in their homes. And protecting their way of life.

2007 brought acquisitions to strengthen our portfolio in the growing telemonitoring area. We acquired Raytel Cardiac Services to expand into US home cardiac monitoring, and by acquiring HealthWatch we are extending our medical alert services, which began with the 2006 acquisition of Lifeline.

Living with heart-related ailments

In addition to providing help in the event of a fall, Lifeline provides extra protection from ailments unrelated to falls – particularly for those coping with heart disease. There are many situations in which someone may need immediate assistance but is unable to call for help themselves: a serious heart arrhythmia, chest pain, difficulty breathing, general fatigue, muscle weakness or other serious forms of distress. Among Lifeline's educational tools is a list of self management tips for heart failure.

Frequent hospital admissions is another common problem for patients with heart failure. That's because managing heart failure at home is a complex task requiring people to remember to take medications, weigh themselves on a regular basis (an indication of fluid retention) and follow a low sodium diet and exercise plan.

Remote patient monitoring

With Philips Telemonitoring Services, clinicians can remotely monitor patients' vital signs data and send them short surveys about their health status. This combination of objective data and subjective responses enables the clinician to make more timely care decisions and helps prevent unnecessary hospitalizations.

Every day, patients take their own vital signs measurements as prescribed by their doctor: weight, blood pressure, pulse, glucose level, blood oxygen level and/or ECG rhythm. They also answer survey questions sent by their clinician, which may include general health assessment questions and/or targeted follow-up questions, and enter self-reported data as directed. The information is then automatically transmitted through an ordinary phone line via modem to secure web-based Clinical Review Software. Clinicians can track daily patient measurements, store and retrieve historical data in both tabular and graphical format, and generate reports – promoting faster follow-up and intervention.

"I yelled for help and thank goodness you heard me. I had congestive heart failure, pneumonia, bronchitis and a minor heart attack…all at once."

Joan D., Lifeline subscriber

40%

Most falls happen at home
Every year seniors fall, but with Lifeline they are never alone

Key strategic acquisition
On December 21, 2007, we announced one of our most important strategic acquisitions in recent years: Respironics, a leading US-based provider of innovative respiratory and sleep therapy solutions. This transaction will firmly place Philips as a global leader in the home healthcare market by adding new product categories in obstructive sleep apnea and home respiratory care to our existing businesses in this field. In addition, this acquisition will be highly complementary to our patient monitoring businesses in the hospital setting.

Respironics is a global leader in the treatment of Obstructive Sleep Apnea (OSA), a condition characterized by the repeated cessation of breathing during sleep. It is estimated that in the United States alone there are 18-20 million sufferers of moderate or severe OSA of which only 15-20% have been diagnosed. Research in recent years has shown a link between OSA, heart disease, stroke and diabetes.

Additionally, the company has a leading position in non-invasive ventilation and has recently introduced new home oxygen technologies to serve the needs of respiratory impaired patients in the home. The remainder of its business is focused on the hospital channel and includes non-invasive and invasive ventilation, respiratory monitoring, neonatal products and respiratory drug delivery technologies for the treatment of respiratory diseases.

There's no place like home

Amsterdam's Sint Lucas Andreas Hospital has implemented our Motiva telemonitoring heart care system, enabling 100 chronic heart patients to be cared for in the comfort of their own homes instead of the hospital. This is the first time such a system has been used outside a clinical trial.

We developed the Motiva personal healthcare platform, which uses broadband technology and vital signs measurement devices to connect patients to their healthcare providers and medical support teams. Patients access personalized content via an easy-to-use interactive television interface. A nurse care manager at the hospital can then monitor the patient's condition, send reminders to take medication, offer lifestyle and diet tips, review data before a doctor's appointment and be alerted if follow-up is necessary. Our partnership with Sint Lucas is a new step in our strategy to increase home healthcare, lower health costs and increase patients' quality of life.

Highlights from our online report

Our online *Sustainability Report 2007* provides detailed information on the four areas below. Also included is the Global Reporting Initiative (GRI) G3 Core Indicators.

www.philips.com/sustainability

Our employees

- The updated version of the Philips General Business Principles Directives was approved and adopted.
- The Employee Engagement Index rose to 64% from 61%.
- The People Leadership Index, which measures 12 aspects relating to one's direct manager, increased to 64% from 59%.
- The percentage of women at executive level rose to 8%, up from 6% in 2006.
- The percentage of women in the top potential pool reached 20%, compared with 18% in 2006.
- The rate of Lost Workday Injuries increased slightly to 0.83 per 100 employees.

Our environmental performance

- Sales from Green Products increased to 20% of total sales, representing an important part of our revenue stream.
- Direct CO_2 emissions from our production processes decreased 2% in 2007.
- We have published for the first time our operational carbon footprint, as seen on page 25.
- In 2007, 11 of our industrial sites purchased green electricity, generated from renewable energy sources. As a result, CO_2 emissions from industrial sites were 3% lower than they would otherwise have been, reducing our operational carbon footprint by 1%.

64%

Engagement survey
Our Employee Engagement Index rose to 64%

20%

Green Products
Sales from Green Products increased to 20% of total sales, representing an important part of our revenue stream

7.7%

EBITA margin
EBITA amounted to EUR 2,065 million in 2007

100%

Transparency
We audited all identified risk supplier sites, achieving our goal of 100% transparency

Our economic performance

- Sales amounted to EUR 26.8 billion representing a 5% comparable growth compared to 2006.
- EBITA as a percentage of sales increased to 7.7% in 2007 from 5.2% in 2006.
- Cash flows from operating activities increased to EUR 1,519 million in 2007 up from EUR 330 million in 2006.
- We proposed to increase the dividend for 2007 by 17% to EUR 0.70 per share.
- We repurchased EUR 1.6 billion of our own shares.
- We announced a further EUR 5 billion (tax-free) share repurchase plan.

Our suppliers

- We are implementing our renewed Supplier Declaration on Sustainability, which aligns with the standards of the Electronic Industry Code of Conduct (EICC).
- We are working to resolve all zero-tolerance issues identified in 2006 supplier site audits. This includes re-audits to ensure sustainable implementation of corrective actions.
- We audited all identified risk supplier sites, achieving 100% transparency of identified risk supplier sites, as well as potential suppliers with identified risk sites.
- As of January 1, 2008, all initial audits will be conducted using the EICC audit profile and we will also audit our own sites.

Appendix
Approach to reporting

Reporting standards
In compiling this report, we have followed relevant best practice standards and international guidelines, including the Global Reporting Initiative's (GRI) G3 Sustainability Reporting Guidelines, which were formally launched in Amsterdam on October 5, 2006. We have sharpened our focus on the principles of materiality, stakeholder inclusiveness, sustainability context and completeness. The results can be seen throughout the report.

With regard to the GRI Application Levels system introduced with G3, we see ourselves currently positioned at the B+ level. We cover a large part of the G3 Core Indicators, while our Management Approach is explained in this report and in our previous sustainability reports. A detailed overview of Core Indicators is provided in our online report.

Scope of this report
This report describes the sustainability performance of the Philips Group, covering the total of the consolidated Philips activities following the consolidation criteria detailed in the *Philips Annual Report 2007*. The Philips Group consists of the following sectors for the reporting year 2007:

- Medical Systems
- Domestic Appliances and Personal Care
- Consumer Electronics
- Lighting
- Innovation & Emerging Businesses
- Group Management & Services.

This report includes selected information on the financial performance of the Philips Group. The consolidated financial statements in the *Philips Annual Report 2007* and the information derived for this report are prepared in accordance with generally accepted accounting principles in the United States (US GAAP).

On November 2, 2007, Philips announced that it has decided to proceed with the sale of its approximate 70% ownership interest in MedQuist. Consequently prior periods' consolidated financial statements have been restated to present the MedQuist business as a discontinued operation. For full understanding of the financial performance, please refer to the *Philips Annual Report 2007*.

Philips is involved in various ventures and participations. The activities of these operations are not consolidated in Philips Group data and are, therefore, not included in this report.

Auditor policy
The company maintains a policy of auditor independence, and this policy restricts the use of its auditing firm for non-audit services, in line with the US Securities and Exchange Commission rules under which the appointed external auditor must be independent of the company both in fact and in appearance. The policy is laid down in the comprehensive policy on auditor independence published on the company's website at www.philips.com

External assurance
Our print report has been externally assured by KPMG, in line with previous reports. Their non-financial assurance engagement, which was conducted in accordance with the the Dutch law, including the Standard 3410N "Assurance engagements relating to sustainability reports," issued by NIVRA, covers all of the information in the report, both quantitative and qualitative. KPMG's Assurance Report, which describes the work undertaken and their conclusions, is on page 67.

Assurance assignment
We have asked KPMG to review the print *Philips Sustainability Report 2007* to provide readers with a reasonable level of assurance on selected financial data, and a limited level of assurance on other information. The report, including the identification of material issues, is our responsibility. Based on the defined scope, KPMG decided to perform the activities described in their assurance report.

Assurance report

To the readers of the print *Philips Sustainability Report 2007*.

Introduction

We have been engaged by Koninklijke Philips Electronics NV (Philips) to provide assurance on the print *Philips Sustainability Report 2007* (further referred to as *The Report*). *The Report* is the responsibility of the company's management. Our responsibility is to issue an assurance report on *The Report*.

Context and scope

In *The Report* Philips describes its efforts and progress in relation to sustainability and reporting thereon. Our engagement was designed to provide the readers of *The Report* with:

- limited assurance on whether the information in *The Report* is fairly stated;
- reasonable assurance on whether the data, as specified in the report section "Our economic performance" are properly derived from the 2007 Group financial statements of Koninklijke Philips Electronics NV, for which KPMG issued an unqualified audit opinion.

Procedures performed to obtain a limited level of assurance are aimed at determining the plausibility of information and are less extensive than those for a reasonable level of assurance.

To obtain a thorough understanding of the financial results and financial position of Koninklijke Philips Electronics NV, the reader should consult the Philips audited Group financial statements for the year ended December 31, 2007.

Reporting criteria

There are no generally accepted standards for reporting sustainability performance. Philips applies its own internal sustainability performance reporting criteria, derived from the Sustainability Reporting Guidelines of the Global Reporting Initiative and internal corporate guidelines for reporting, as detailed on page 68-69 of *The Report*. It is important to view the performance data in the context of this explanatory information. We believe that these criteria are suitable in view of the purpose of our assurance engagement.

Standards

We conducted our engagement in accordance with Dutch law, including Standard 3410N "Assurance engagements relating to sustainability reports." This standard requires amongst others that the assurance team members possess the specific knowledge, skills and professional competencies needed to understand and review the information in *The Report*, and that they comply with the requirements of the IFAC Code of Ethics for Professional Accountants to ensure their independence.

Work undertaken

With regard to the information in *The Report* we carried out the following activities:

- reviewing the systems and processes for information management, internal control and processing of the other information;
- reviewing the data reported by all EcoVision reporting organizations and the data validation processes at corporate and product division level;
- visiting 3 reporting organizations to assess the data collection and reporting process and review the reliability of the reported data;
- discussing the results of the internal audits carried out by Philips;
- reviewing data trends and discussions with management thereto;
- interviewing staff responsible for the analysis and reporting of the data and accompanying notes for these indicators;
- reviewing internal and external documents to determine whether qualitative information is supported by sufficient evidence;
- an assessment of the plausibility of the assumptions underlying the prospective information.

For the financial data we have reconciled the data on financial performance in the section "Our economic performance" of the *Sustainability Report 2007*, with the audited 2007 Group financial statements of Royal Philips Electronics.

Following our review we discussed changes to the draft Report with Philips, and reviewed the final version of *The Report* to ensure that it reflected our findings.

Conclusion

Based on the above,

- the information in *The Report* does not appear to be unfairly stated;
- the data, as specified in the report section "Our economic performance" are properly derived from the 2007 Group financial statements of Koninklijke Philips Electronics NV, for which KPMG issued an unqualified audit opinion.

Commentary

Without affecting the conclusions presented above, we would like to draw readers' attention to the following:

With the EcoVision4 program Philips has further emphasized its role in the total value chain. Philips has set targets on innovation, operational energy efficiency and sales of Green Products.

At present parts of the reporting systems for these targets need further development. Also it is not yet possible to deliver fully reliable data for activities that are not under Philips' direct control (such as distribution). In order to be able to closely monitor the performance on the targets set and to identify opportunities for improvements we recommend Philips to further improve the quality of the reporting systems for the relevant performance data.

Philips has started to further focus on its impact on climate change. The information regarding the operational carbon footprint has partly been collected for group reporting purposes. In order to show the full impact of Philips' efforts on climate change and to be able to manage this, we recommend Philips to further embed operational carbon footprint reporting into the business and to find ways to further demonstrate the impact of Philips' green product developments on carbon emissions.

Amstelveen, February 18, 2008

KPMG Sustainability B.V.
Drs. W.J. Bartels RA (director)

Explanatory notes

Scope of reporting

The general scope of reporting performance data for the Philips Group is described on page 66. The scope of reporting for our operational carbon footprint, health and safety, environmental performance and supplier sustainability is described below.

Comparability

For manufacturing data, the Semiconductors division is excluded from the year totals for the Philips Group for all years, unless otherwise stated.

All data are reported in absolute terms.

Portfolio changes in 2007

The main divestments with manufacturing activities in 2007 were various Optical Storage sites and CE Mobile phones in China. Data from these organizations are not included in 2007 reporting.

Major acquisitions in 2007 were PLI (Lighting), Color Kinetics (Lighting), VMI (Medical Systems), LTI (Lighting) and DLO (CE).

Operational carbon footprint

Scope

The Philips operational carbon footprint includes:

- Industrial: manufacturing and assembly sites.
- Non-industrial: offices, warehouses, IT centers and R&D facilities.
- Business travel: lease and rental cars, train and airplane travel.
- Distribution: air, sea and road transport.

All conversion factors used to transform input data (e.g. amount of ton-kilometers) into CO_2 emissions are from the Greenhouse Gas Protocol. This Protocol distinguishes three scopes, the first two of which are mandatory to report on. We cover:

- Scope 1 – direct CO_2 emissions – is completely reported on with direct emissions from industrial and non-industrial sites.
- Scope 2 – CO_2 emissions resulting from the generation of purchased electricity – is completely reported on with electricity use from industrial and non-industrial sites.
- Scope 3 – other CO_2 emissions related to activities not owned or controlled by the company (optional category) – is reported on with business travel and distribution. Commuting, upstream distribution, outsourced activities and emissions resulting from product use are not included.

Methodology

CO_2 emissions from industrial sites are reported in the EcoVision reporting system, which consists of direct emissions resulting from processes and fossil fuel combustion on site, and indirect emissions from purchased electricity, steam and heat. Emissions from industrial sites that are not yet reporting in EcoVision (see "Environmental performance" explanatory notes on page 69) are calculated. The calculation is based on average CO_2 emissions per square meter of sites from the same sector. CO_2 emissions from non-industrial sites are not reported in EcoVision but are calculated. This is done by calculating the energy use per square meter for six countries in Europe and multiplying this factor to the square meters of the remaining sites. The reference year for these data is 2007.

The calculations for business travel by lease and rental cars are based on kilometers and fuel usage. Emissions from business travel by airplane are calculated from the number of kilometers flown. For business travel by train currently only the spend is registered. CO_2 emissions were calculated from distance traveled, based on an estimate of the average distance per euro spent. Even though this is not highly reliable, it has no significant impact, being less than 0.1% of on the total carbon footprint. The reference year for this part of the scope is a mixture of 2006 and 2007, because 2007 data were not always available.

Emissions from air freight for distribution are calculated based on the amount of ton-kilometers transported between ports (distinguishing between short, medium and long hauls for air transport). Because for sea transport only data on transported volume were available, an estimate had to be made about the average weight of a container. Transportation to and from ports is not registered. This fore and aft part of air and sea transport was estimated to be around 3% of the total distance, consisting of a mix of modalities, and was added to the total emissions accordingly. Finally, road transport is the modality with the highest amount of uncertainty. Where data were available, CO_2 emissions were calculated based on distances and fuel use, or on ton-kilometers. If data were incomplete, the emissions were estimated based on average

distances and spend. For this part of the scope the reference year was 2006.

Health and safety

Basis for reporting

Data are reported on a monthly basis and validated on a half yearly basis.

Accounting for organizational changes

Data for new reporting organizations that started reporting in the current reporting year are added to the divisional and thus company totals in the first quarter they are consolidated.

Data for reporting organizations that were divested in the current reporting year are taken out of the divisional and thus company totals in the first quarter they are deconsolidated.

Completeness

Data reported over 2007 cover 80% of the total number of Philips' FTEs. We aim for 100%. The difference can be explained by:

- Non-reporting of Medquist in the US and Shenyang in Asia Pacific region.
- Newly consolidated organizations not yet reporting include Avent Holdings, Color Kinetics, Intermagnetics, PLI, Lifeline. Systems, Lighting Bodine, LTI Lighting, Lumileds.
- Some non-reporting organizations in the Netherlands.
- A number of small units.

Environmental performance

Environmental reporting standard

All reporting instructions, including definitions, procedures, calculation methods, etc., are included in the intranet-based EcoVision reporting and validation system.

Basis for reporting

The environmental data in this report have been provided by our environmental reporting organizations. The following consolidation criteria have been applied:

- New acquisitions are reported after the first full year, therefore acquisitions from 2007 will be included in the reporting for 2008.
- Data for divestments that take place during the reporting year are not included.
- Environmental data are reported by each manufacturing activity owned, rented or leased and managed by Royal Philips Electronics, with 50 or more people working in production, and which is consolidated for financial reporting by Royal Philips Electronics.

Various acquisitions in 2005-2006 have not yet been included due to management decisions: Intermagnetics (Medical Systems), Lumileds (Lighting); Avent Holdings (DAP); Lighting Bodine (Lighting); FeiXin (Lighting), which started reporting in 2007 as a reference year but not considered in Group totals. Reporting for these units will begin in 2008.

Accuracy

The conversion factors used for direct energy and restricted substances are unchanged from 2005. The conversion factors of direct Global Warming Potentials (GWP) were updated according to IPCC Third Assessment Report (TAR-06) and the conversion factors of indirect grams CO_2/kilowatt hour (kWh), which is taken from the International Energy Agency Data Services "CO_2 Emissions from Fuel Combustion (2006 Edition)."

We will update our software and reporting manual to reflect changes resulting from information in "Climate Change 2007," the Intergovernmental Panel on Climate Change (IPCC) 4th Assessment Report, published in 2007.

Completeness

Of the 100 reporting organizations four did not report. The influence of the missing data on corporate level is negligible.

Furnaces at Lighting sector production sites produce direct CO_2 emissions due to the decarbonization of dolomite and other carbonates. These emissions have not yet been included in our EcoVision reporting for manufacturing activities. We have estimated that they represent between 9% and 10% of total direct CO_2 emissions related to manufacturing activities, and this is included in our operational carbon footprint. We will adjust our reporting systems in 2008 to include these emissions.

Comparability

The reference year for the EcoVision III program is 2005, therefore no data changes are applicable for the years 2002-2004.

Supplier sustainability

Identified risk suppliers are defined as follows:

- We idenfied risk countries based on the Maplecroft list.
- Suppliers from those identified risk countries with whom we also spend more than EUR 100,000 are identified as risk suppliers.
- Suppliers of new ventures are included to the extent that the integration process of these ventures has been finalized. Normative integration period is two years after closure of the new venture.

Reporting standards

All reporting instructions, including definitions, procedures, calculation methods, etc., are available on our website www.philips.com/sustainability

Glossary

Carbon footprint The measure of carbon dioxide produced by a person, organization or state in a given time.

CE Philips Consumer Electronics, combined with DAP in the Philips Consumer Lifestyle sector.

CFC Chlorofluorocarbon – CFCs are considered deleterious to the ozone layer.

CO_2 Carbon dioxide – The most prevalent greenhouse gas.

CT Computed tomography – A special radiographic technique that uses a computer to assimilate multiple X-ray images into a two-dimensional cross-sectional image.

DAP Philips Domestic Appliances and Personal Care, combined with CE in the Philips Consumer Lifestyle sector.

EICC The Electronic Industry Code of Conduct identifies appropriate standards of conduct for socially responsible entities operating in the electronics industry. www.eicc.info

EMS Part of an organization's general management system, an environmental management system makes it possible to formulate clear goals for environmental work, systematic follow-up of results and documentation of practices and activities.

EU European Union – Formerly known as European Community or European Economic Community, this is a union of 27 independent states based on the European Communities and founded to enhance political, economic and social cooperation. europa.eu

FTE Full-time equivalent – A figure calculated from the number of full-time and part-time employees in an organization that represents these workers as a comparable number of full-time employees.

GHG Protocol The Greenhouse Gas Protocol is the most widely used international accounting tool for government and business leaders to understand, quantify and manage greenhouse gas emissions. The GHG Protocol Initiative, a decade-long partnership between the World Resources Institute and the World Business Council for Sustainable Development, is working with businesses, governments, and environmental groups around the world to build a new generation of credible and effective programs for tackling climate change. www.ghgprotocol.org/

GJ Gigajoule – The joule (J) is the basic energy unit of the International System of Units (SI). It is ultimately defined in terms of the meter, kilogram and second. Giga is the metric prefix indicating 10^9 times base unit (1 followed by 9 zeros).

Global warming The gradual increase of the warming temperature of the earth's lower atmosphere as a result of the increase in greenhouse gases since the Industrial Revolution. Sustained increase causes climatic changes.

GRI Global Reporting Initiative – A worldwide, multi-stakeholder network the GRI's vision is that reporting on economic, environmental and social performance by all organizations is as routine and comparable as financial reporting. www.globalreporting.org

HCFC Chlorofluorocarbon containing one or more hydrogen atoms. HCFCs are an alternative to CFCs, with approximately one-tenth of their ozone-depleting properties and greenhouse effect.

IPCC The Intergovernmental Panel on Climate Change – Established by the World Meteorological Association (WMO) and United National Environment Programme (UNEP) to assess scientific, technical and socio-economic information relevant for the understanding of climate change, its potential impacts and options for adaptation and mitigation. www.ipcc.ch

ISO 14001 Formulated by the International Standardization Organization (ISO) this standard forms the basis for setting up, auditing and certifying Environmental Management Systems. www.iso.org

KPI Key Performance Indicator – Financial and non-financial metrics used to quantify objectives to reflect strategic performance of an organization.

NGO Non-governmental organization – A not-for-profit organization that pursues an issue or issues of interest to its members by lobbying, persuasion and/or direct action.

PET Positron emission tomography – A highly specialized imaging technique that uses short-lived radioactive substances to produce three-dimensional colored images of those substances functioning within the body.

PJ Petajoule – The Joule (J) is the basic energy unit of the International System of Units (SI). It is ultimately defined in terms of the meter, kilogram and second. Peta is the metric prefix indicating 10^{15} times base unit (1 followed by 15 zeros).

Sustainable Development This concept was first conceived in 1987 by Gro Harlem Bruntland, the premier of Norway, who led the World Commission on Environment and Development. Its report, titled Our Common Future, defined Sustainable Development as "meeting the needs of the present generation without compromising the ability of future generations to meet their own needs."

UN United Nations – Established in 1945, the purposes of the United Nations, as set forth in its Charter, are to maintain international peace and security; to develop friendly relations among nations; to cooperate in solving international economic, social, cultural and humanitarian problems and in promoting respect for human rights and fundamental freedoms; and to be a centre for harmonizing the actions of nations in attaining these ends. www.un.org

UNFCCC The United National Framework Convention on Climate Change secretariat supports all institutions involved in the climate change process, particularly the Conference of Parties (which meets once a year to review the Convention's progress), the subsidiary bodies and their Bureau. www.unfccc.int

US GAAP United States Generally Accepted Accounting Principles

WBCSD The World Business Council for Sustainable Development is a CEO-led, global association of some 190 companies dealing exclusively with business and sustainable development. www.wbcsd.org

WHO World Health Organization – The United Nations specialized agency for health, established in 1948. WHO's objective, as set out in its Constitution, is the attainment by all peoples of the highest possible level of health. www.who.int

World Bank The World Bank provides financial and technical assistance to developing countries. It is comprised of two unique development institutions owned by 185 member countries – the International Bank for Reconstruction and Development (IBRD) and the International Development Association (IDA). www.worldbank.org

Our employees

The wide world of Philips

More than 120,000 Philips people in approximately 150 countries work together to create and sell new products and technologies. They brainstorm, research and develop. They build, market and service. In short, we touch people's lives every day.

Our employees

The number of Philips employees at year-end 2007 totaled 123,801, an increase of 2,069 compared to the previous year. Additional headcount from acquisitions completed during the year (notably in Lighting and Medical Systems) was partially offset by divestments of businesses (mainly Optical Storage and the Finance Shared Services operations).

These changes in the Philips portfolio had – on balance – a positive effect of 3,119 on the total numbers of employees. On a comparable basis, the headcount decreased by 1,050 persons. Reduced employment levels at Consumer Electronics and Innovation & Emerging Businesses were partly offset by increases at Lighting and Medical Systems.

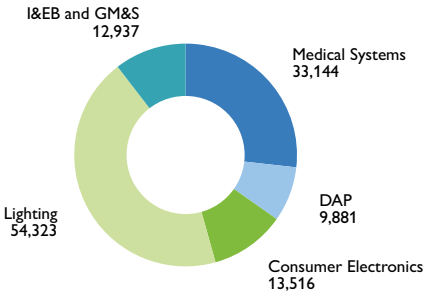
Philips General Business Principles

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 intention of the GBP is to ensure compliance with laws and regulations, as well as with Philips' norms and values.

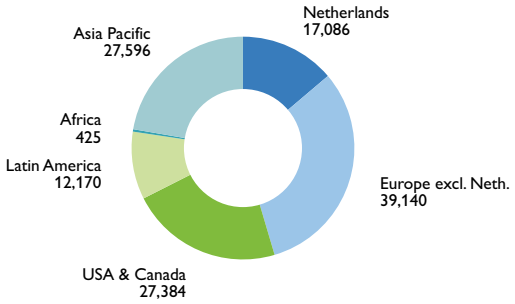
The GBP are available in most of the local languages and are an integral part of the labor contracts in virtually all countries where Philips has business activities.

Responsibility for compliance with the principles rests principally with the management of each business.

Employees by sector at year-end 2007
in FTEs



Employees by geographic area at year-end 2007
in FTEs



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 Line ensures that alleged violations are registered and dealt with consistently within one company-wide system. In 2007 the French privacy authorities granted approval for the roll-out of the hotline in that country (completed in November). In Germany the workers' representation bodies also approved the introduction of a hotline. These approvals now ensure comprehensive company-wide implementation.

To drive the practical deployment of the GBP, a set of directives has been published, including a Supply Management Code of Ethics and a Financial Code of Ethics (www.philips.com/about/investor). In 2007, the updated version of the GBP Directives was approved and adopted, reflecting ongoing developments in codes of conduct and business integrity legislation. The main updates related to Philips' endorsement of the UN Global Compact, policy on HIV/AIDS, health and safety policy, integrity and ethics in advertising, and in particular directives on the giving of gifts. To ensure compliance with the highest standards of transparency and accountability by all employees performing important financial functions, the Financial Code of Ethics contains, amongst other things, standards to promote honest and ethical conduct, and full, accurate and timely disclosure procedures to avoid conflicts of interest. The Company did not grant any waivers of the Financial Code of Ethics in 2007.

In order to publicize the updated GBP Directives, a global internal communications program was rolled out in the first half of 2007, with participation of the Board of Management and Group Management Committee and the respective Area and Country Management.

A company-wide toolkit has been developed and rolled out in 2007 for the compulsory registration of gifts to third parties to ensure full transparency in monitoring compliance with company standards.

To reinforce awareness of the need for compliance with the GBP, a web-based GBP training tool has been rolled out throughout the company in 22 different languages, covering more than 95% of the employees with online access.

The e-training program for (new) compliance officers (including complaint-handling procedures and dilemma training) was updated in 2007. Furthermore, 2007 saw the development and worldwide roll-out of a train-the-trainer program for compliance awareness. Two-day training sessions were held in Latin America, Asia Pacific and Europe, with the remaining sessions scheduled for the first quarter of 2008. This program provides for an annual refresher course.

General Business Principles: reported complaints

In 2007 a total of 389 concerns were raised, compared with 392 in 2006 and 318 in 2005. As many of the alleged violations are currently still being investigated, it is impossible to determine exactly which – if any – General Business Principles have been infringed and to what extent. However, on the basis of the preceding analysis, it is possible to draw some conclusions about those GBP that are most frequently called into question.

The trend we have seen over recent years towards a sharp increase in the number of reported (alleged) violations relating to working conditions – GBP 4 – (29.0% of the total in 2004, 48.1% in 2005 and 58.8% in 2006) fell somewhat in 2007 to 55.8%. It would seem

that in terms of the reporting of HRM issues the maximum effect of the extended scope of the GBP (effective 2005) has been achieved, especially in the employee domain and given the completion of the roll-out of the One Philips Ethics hotline (in 2006).

In contrast to the HRM issues, where the rising trend fell slightly, in the case of the archetypal Business Integrity issues the opposite was the case. The strong relative decrease in alleged violations of GBP 7 (bribery; records of transaction; third party interests; political payments) came to an end in 2007. The fall from 31% of the total in 2004 to 13.7% in 2005 and 10.9% in 2006 was reversed in 2007 when the figure rose again to 17.2%. This is not attributable to a more relaxed internal control environment or reduced awareness within the Philips organization, but completely due to the effect mentioned earlier of a more critical and detailed evaluation of the alleged violations, which has led to a shift from the Others to the Fraud category.

In 2007 there was a clear decline in the number of complaints relating to supply management. Only nine complaints were logged in the GBP Complaints database as alleged violations of GBP 5 (Commitment to Suppliers and Business Partners) compared with 23 in 2006. The sharp fall compared with 2006 is due to a large degree to the high number of supplier assessments held in the risk countries China, Brazil, India, Philippines, Mexico, Indonesia, Thailand, Korea, Malaysia and the focus on the resolution of the major non-compliances (i.e. the zero-tolerance and limited-tolerance violations) that came to light during these assessments.

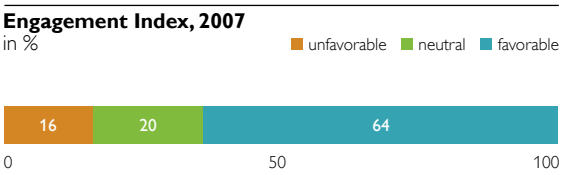
In 2007 again the GBP most associated with alleged violations was GBP 4.3 (Equal and fair treatment), although in both relative and absolute terms there has been a slight fall (44.3% as opposed to 47.1% in 2006). The other GBP most likely to have been infringed were

Breakdown of alleged violations of the General Business Principles

as a % of total

Chapters		2004	2005	2006	**2007**
1	General commitment				
1	General commitment	6.3	2.2	4.5	**3.2**
1.1	Human rights	0.0	0.0	0.0	**0.0**
1.2	Child, bonded and forced labor	0.0	0.0	0.0	**0.0**
1.3	Free market competition	3.0	0.0	0.0	**0.5**
1.4	Product safety	0.4	1.1	0.7	**0.5**
1.5	Privacy	0.4	0.5	1.7	**2.8**
1.6	Environmental protection	0.0	0.5	0.3	**0.0**
	Total	10.1	4.3	7.2	**7.0**
2	Commitment to customers				
	Total	1.9	0.0	1.2	**0.7**
3	Commitment to shareholders				
	Total	0.4	0.0	0.3	**0.0**
4	Commitment to employees				
4	Commitment to employees	2.6	6.7	2.2	**2.8**
4.1	Right to organize	0.0	1.1	0.5	**1.5**
4.2	Health and safety	0.7	1.6	5.0	**2.5**
4.3	Equal and fair treatment	26.1	34.1	47.1	**44.3**
4.4	Wages and payment	0.0	4.6	4.0	**4.7**
	Total	29.4	48.1	58.8	**55.8**
5	Commitment to suppliers and business partners				
	Total	0.0	8.9	5.7	**2.3**
6	Assets and information				
6.1	Use and protection of assets	23.9	19.6	12.6	**15.5**
6.2	Improper disclosure	3.0	4.6	3.0	**1.5**
6.3	Insider trading	0.0	0.0	0.0	**0.0**
	Total	26.9	24.2	15.6	**17.0**
7	Business integrity				
7.1	Bribery; records of transaction	20.1	11.0	10.4	**14.5**
7.2	Third-party interests	11.2	2.2	0.5	**2.0**
7.3	Political payments	0.0	0.5	0.0	**0.7**
	Total	31.3	13.7	10.9	**17.2**
8	Observance of the General Business Principles				
8.1	Sanctions	0.0	0.0	0.0	**0.0**
8.2	Whistleblower policy	0.0	0.8	0.3	**0.0**
8.3	Compliance	0.0	0.0	0.0	**0.0**
	Total	0.0	0.8	0.3	**0.0**
	Overall total	100.0	100.0	100.0	**100.0**

Engagement Index, 2007
in %



Source: Philips Employee Engagement Survey 2007
Number of responses: 90,726

GBP 6.1 (Use and protection of assets), which came second with 15.5%, and GBP 7.1 (Bribery; records of transactions), which came a close third with 14.5%. This means that the top three have remained unchanged over the years.

A clear focus

To help employees reach their full potential and to help the company achieve its growth objectives, in 2007 we continued to focus on boosting engagement and improving talent management.

Engaging for growth

Almost 91,000 employees – from across all sectors and functions – gave their answers to the same 39 questions on leadership, management capabilities, line of sight and alignment with the company's vision, identification with the brand, communication, reward and recognition, and diversity and inclusion.

The response rate of 92%, up from 85% last year, is the highest ever.

Engagement Index

If we were to sum up the results of the Engagement Survey in one figure it would be the Employee Engagement Index (EEI). This includes responses to three items on satisfaction, referral and loyalty.

Moving closer to the High-Performance norm

The EEI increased to 64% in 2007 from 61% the previous year. The High-Performance (HP) norm – the score achieved by the top 25% of companies from our partner Kenexa's database – is 70%.

Philips has set itself the goal of reaching the High-Performance norm by 2009. So while we are on the right track, the remaining gap still needs to be closed. The trends are encouraging, but we recognize there is room for further improvement.

A look at the results

While many scores were higher than last year, there are still a number of areas that can be improved, especially when measured against the High-Performance norm. For example, while "Proud to work for Philips," scored a respectable 72%, this is 10 points lower than the HP norm.

However, on the "Open and honest two-way communication," the "Trust in leadership" or a "Climate in which diverse perspectives are valued," we are at or above the HP norm.

There is, moreover, a significant improvement in the "Vision of the future that motivates me," steadily increasing from 50% in 2005, to 56% in 2006, and up to 61% in 2007, which is almost the HP norm of 63%.

Creating a dialogue

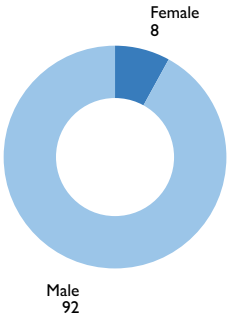
Detailed reports of the survey results were sent to every manager with a team of eight or more people – some 3,500 in total. In "Deep Dive" sessions, running from November 2007 until the end of March 2008, teams talked about their results, discussing strengths and weaknesses, and putting corrective actions into place to address areas of concern.

About 600 critical "Deep Dives" will be tracked and monitored by 300 specially trained HR generalists. We believe it is important that everyone take responsibility for proactively following up on the survey at a local level, creating a dialogue between and among leaders and team members.

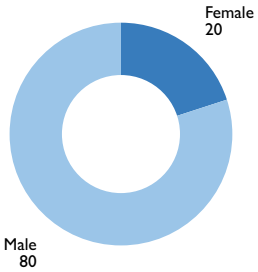
Outlook

We plan to implement a number of changes to the 2008 survey to better link engagement to the key performance objectives we have for Philips as part of Vision 2010, our ambitious growth plan for the coming years, as well as the essential behaviors

Composition of Philips executives (total=489) at year-end 2007
as a % of total



Composition of Philips top potentials at year-end 2007
as a % of total



we expect our leaders to demonstrate to drive this growth.

Diversity & Inclusion

Our vision is of one company made up of many different faces. A company with a more diverse range of people and an inclusive workplace environment where differences are honored, respected and encouraged.

Truly connecting with the people who buy our products means doing more than analyzing the changes going on in the world – the growth in Asia and Central and Eastern Europe, the growing spending power of working women, demographic changes for example – we need to be a real part of these changes, reflecting our markets.

Diversity & Inclusion, a function within Philips' Corporate HR department since 2004, has been working closely with other HR functions and our businesses to embed into D&I in existing processes like recruitment and talent development and to help instill an inclusive climate within the Philips culture.

To ensure we reach our goals to increase the percentages of women and other under represented groups in senior management positions. D&I Champions for every business and region provide a vital link between the businesses and regions, and the corporate D&I team. Most Champions have a day to day role in Management development, thus forming a vital link between D&I on the one hand and talent pipeline development and succession planning on the other.

Raising awareness

In 2005, we started with D&I Workshops for employees including Management levels worldwide. This ongoing activity was continued in many places around the world during 2007.

WINergy, our women's network, seeks to raise awareness of women's needs within the company's top management, support and mentor women in member's teams and share information. WINergy started at executive level 2004. In 2007, regional and local "chapters" were added to the WINergy network. These chapters are connected via an online community. At year-end WINergy had 10 chapters, uniting approximately 400 Philips women at different job levels and from different parts of the world.

In August 2007, Philips co-sponsored in an inter-company Company Pride conference for the gay, lesbian, bisexual and transgender (GLBT) community for the first time. We are currently exploring follow up actions with representatives of the GLBT community within Philips.

In 2007 we also took further steps to regionalize D&I. A focus group was established in the United States to explore specific actions that fit under our global D&I umbrella, but are adapted to US culture and legislation. Philips Latin America has established its own D&I Policy. Early 2008, we will begin exploring specific needs and subsequent action plans for Asia.

Making progress

As in previous years, we are continuing to focus on increasing the opportunities for women and other under-represented groups in key positions, and on developing a diverse talent pipeline.

We want to increase the percentage of women in executive positions. The percentage of women at executive level rose to 8% in 2007, up from 6% the previous year. The percentage of women in the top potential pool was reached 20% in 2007, compared with 18% in 2006.

We want to increase the percentage of Asians in key executive positions. The percentage of Asian executives remained stable at 7% in 2007, while the percentage top potentials from Asia Pacific was 16% a decrease from 18% in 2006.

Developing our people

In a move to develop local talent, during 2007 we shifted the responsibility for the attraction and development of talent up to and including high potentials to the countries. We see this as critical to growing people and the company.

Global Learning Curricula

Employees across the world can access detailed information about our Global Learning Curricula and register for courses online via our Global Learning Portal, "Learning @ Philips". They can find learning programs to develop themselves and others in a user-friendly One Philips platform.

With nearly 12,000 employees participating in programs in the Core Curriculum during 2007, enrollment remained steady compared with the previous year. Our Core Curriculum offers learning opportunities in the areas of personal effectiveness, people management and business acumen.

Our Functional Core Curricula includes courses in Finance, HRM, IT, Sales, Marketing, Project Management and Supply Management. Enrollment in the Functional Core Curricula was some 8,000 in 2007, nearly double the 2006 number. Many Functional Curricula are tied to mandatory learning plans designed to increase our organizational capability.

Talent Pipeline Curriculum

The Talent Pipeline Curriculum consists of systematic, accelerating and inspiring learning interventions for the Philips talent pool (from high potentials to executives). Our advanced learning experience for high potentials, called Inspire, is designed to develop future leaders who are able to combine a thorough understanding of their business environment with excellent personal skills. The Octagon program is the accelerating development program for top potentials, offering participants the opportunity to use the strategic insight, knowledge and skills required to tackle a major (cross-sector/cross-regional/cross-functional) issue, and round out their Philips leadership behavior.

We conducted eight project assignments for Inspire and another eight for Octagon, all closely tied to growth. One of our Inspire teams, for example, went to Tanzania to explore business development opportunities. These teams consisted of participants from across divisions, regions and functions.

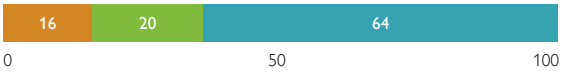
Executive education

To help our executives to continue to develop their careers and strengthen their leadership skills, we offer a curriculum of internal and external programs. The preferred external programs have been used increasingly, with approximately 9% of executives and confirmed top potentials attending these programs in 2007.

Our Master Classes on people management topics include our Master Class Engaging for Performance, which is designed for executives and senior teams. We organized more than 40 classes in 2007.

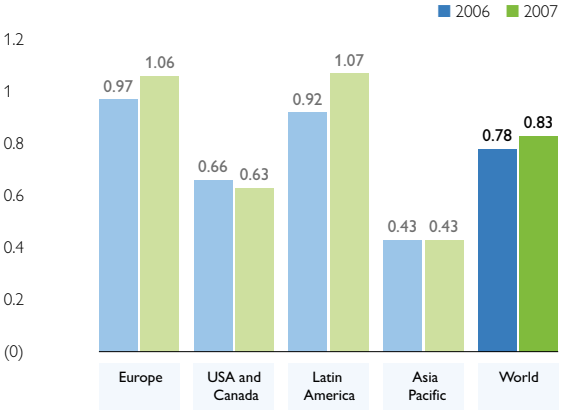
We redesigned our executive induction program for newly hired or recently appointed executives. The first run was successful and 23 executives participated in 2007. We plan to run this program twice during 2008.

People Leadership Index, 2007
in %



Source: Philips Employee Engagement Survey 2007
Number of responses: 90,726

Lost Workday Injuries by region
per 100 FTEs



People Leadership Index

Because managers contribute significantly to the engagement of their employees, we have developed the People Leadership Index (PLI), which focuses on overall people leadership effectiveness. Our PLI – measuring 12 aspects relating to management capabilities – rose to 64% in 2007 from 59% in 2006. This is an encouraging result, as it shows that our efforts to improve our managers' leadership skills are paying off.

Health and safety

Philips strives for an injury and illness free work environment. To drive improvement we set performance goals for the company and our individual sectors.

Occupational health and safety is an integral part of our business activities and management systems. Many Philips sites have a certified Occupational Health and Safety Management System according to the OHSAS 18001 standard.

We are no longer including illness rates (Lost Work Time rate) as we did in previous reports, in view of significant regional and country differences due to legislation, cultural differences and alignment with local reporting requirements. Rather, we are sharpening our focus on occupational injuries.

Lost Workday Injuries

In 2007 we recorded 817 Lost Workday Injuries, occupational injury cases where the injured person is unable to work the day after the injury. Lost Workday Injuries reported in 2006 amounted to 829. The rate of Lost Workday Injuries was 0.83 per 100 FTEs (full-time equivalents). We consider this level of injuries to be too high compared with industry benchmarks.

As the charts illustrate, there are significant differences by geography due to differences in legislation and culture.

Most of the occupational accidents occur in the Lighting sector (68%), which represents the majority of our worldwide manufacturing activities. Lighting management has committed itself to driving improvement with a program to reduce the frequency and severity of occupational accidents.

This three-year program (2008-2010) will focus on management leadership; updating safety standards; promoting a safety culture, awareness and safe behavior; and sharing of best practices. The program roll out has started in the Lighting business group Lamps, with other business groups to follow in the coming years. The first results are expected in 2008-2009.

Our environmental performance

Key global challenges

The significant issues for our company – and our industry – in the environmental area continue to be energy efficiency, chemical content of products, and take-back and recycling. We remain committed to giving our full attention to these challenges. At the same time we are maintaining our focus on overall environmental performance improvement, driven by our EcoVision III action program, as well as our EcoVision4 program, which is detailed on pages 23-25.

Energy efficiency

The European Commission continues its sharp focus on energy efficiency of products with its Energy Efficiency Action Plan. As a major step toward meeting the energy challenges facing the European Union, the plan calls for "saving 20% by 2020."

Two of the mechanisms for achieving this goal relate to our business: the EU directive on the eco-design of energy-using products (EuP) and the EU energy labeling directive.

EuP aims at improving the environmental performance of products throughout their life-cycle by systematic integration of environmental aspects at the earliest stage of their design. Studies were initiated in 2006 that will lead to legal requirements on specific products and sectors.

Philips represents the consumer electronics/information and communications technology industry on the Stakeholder Consultation Forum, which provides input on drafts that go to the EU's regulatory committee and eventually to the European legislative institutions, to be passed as legislation under the EuP umbrella. The EU held the first stakeholder consultation meetings in 2007 focusing on items ranging from street lighting to standby power. Final legal measures are likely to be published in the next year.

The EU energy labeling directive applies to such products as refrigerators, washing machines and lamps. This will likely expand to new product sectors, considering that consumer electronics are the fastest growing type of products in people's homes and will be the largest by 2010. The EU laid out its plans to use EuP and energy labeling to further enhance energy efficiency in an increasing number of industry sectors.

Other countries, including the United States and Australia, are also gearing up to decrease energy usage and contribute less to global warming through legislative measures, as discussed on pages 32-33.

For details about "Philips and energy efficiency" please see pages 26-45.

Chemical content of products

To ensure human health and protect the environment, the EU has been working to prevent pollution from sources as diverse as lead in gasoline and chemicals in batteries. Recent legislation focusing on chemical substances is underpinned by the precautionary principle.

At Philips we have long been guided by the precautionary principle, adopted by the UN Conference on Environment and Development in Rio de Janeiro in 1992. The principle states that in order to protect the environment, a precautionary approach should be widely applied, meaning that where there are threats of serious or irreversible damage to the environment and/or health, lack of full scientific certainty should not be used as a reason for postponing cost-effective preventive measures.

Simply put, our philosophy is that "prevention is better than cure."

We have an extensive list of restricted substances that are banned from our products, along with another list of chemicals banned during production processes. In addition we have a list of hazardous substances, which we strive to significantly reduce or eliminate, and a list of relevant substances, to which we pay attention from a precautionary point of view.

The Royal Philips Electronics List of Restricted Substances is also part of our Purchase Agreements. This is an important element of our Supplier Sustainability Involvement Program.

Polyvinyl Chloride

Polyvinyl Chloride (PVC) is still in widespread use as packaging material today since it is cheaper and easier to use than the alternatives. We banned PVC from product packaging in the mid-1990s.

The typical use for PVC is blister packs for small products. First, by using other blister pack materials than PVC, Philips has eliminated much more PVC then what remains in the small product typically in the form of cables. Second, while PVC in a product does not necessarily cause problems when users return their end-of-life products to a well-equipped electronics recycling system, PVC from packaging can "go astray" and end up in the environment in an uncontrolled way, or be improperly treated during packaging recycling. It simply makes sense for us to be rigorous about PVC-free packaging.

In 2008 we will continue to investigate options to replace PVC in products.

Brominated Flame Retardants (BFRs)

All Philips products are designed with quality and safety in mind. In some cases there can be a conflict between safety regulations and environmental impact reduction.

In 1998 we began proactively restricting the use of cadmium, mercury and PBBs/PBDEs in many product

categories. We are compliant with RoHS, which bans the placing on the EU market of new electrical and electronic equipment containing more than the agreed levels of the heavy metals cadmium, lead, mercury, hexavalent chromium, and flame retardants polybrominated biphenyls and some polybrominated biphenyl ethers.

For some products, like televisions, we have chosen to pre-empt safety standards that will not come into effect for years. Since 2003 housings of all Philips FlatTVs have been flame retardant globally – although this is not required in most regions of the world. Moreover, we are doing this on the basis of non-brominated flame retardants, an explicit choice with the environment in mind. Few TV manufacturers follow the same path, since this choice represents a high investment. At Philips we believe that this is another example how a company can make products that are better for both the user and the environment.

The amount of bromine avoided by choosing non-brominated flame retardants far outweighs the amounts of bromine still present in the printed circuit boards of these products. To plan for an eventual phase-out of BFRs, we will continue to research alternative materials for bromine in printed circuit boards and will transition to such materials when these become available, are economically feasible and will not negatively impact product reliability and safety. We will also continue to evaluate the type of flame retardants used in product housings depending on market and scientific developments.

In 2008 we will continue to investigate options for alternatives for BFRs.

Developing industry lists

We were at the forefront in the early 1990s in developing common lists used by electronics companies through the European industry association, then called EACEM.

More recently, we have been engaged in such activities as a global initiative to construct one list of chemicals of concern for electronics products, or standardization activities to define workable ways to sample and test electronics products for substances banned under the EU Directive on the restriction of the use of certain hazardous substances in electrical and electronic equipment, known as RoHS, which went into effect on July 1, 2006.

RoHS

Our global policy applies the EU RoHS requirements to all of the markets we serve. While medical equipment is currently not in the scope of the RoHS legislation, our Medical Systems division is proactively eliminating these substances where possible.

Legislation around the world is not fully harmonized, making it necessary to deal with differences on a regional basis. This can result in regional deviations from our global policy for specific product types.

Philips continues to play a leading role in setting international standards on compliance and understanding of RoHS, working in close cooperation with the International Electrotechnical Commission (IEC). The IEC prepares and publishes international standards for all electrical, electronic and related technologies. These serve as a basis for national standardization and as references when drafting international tenders and contracts. We have representatives on several IEC technical committees related to regulated substances.

REACH

The European Union's REACH Regulation (registration, evaluation and authorization of chemicals) entered into force on June 1, 2007.

"We incorporate design-for-recycling into our overall EcoDesign process."

Under REACH, producers and importers of chemicals will be required to register an estimated 30,000 substances in a central database, providing information about the chemicals' properties, effects and uses, and safe ways of handling them. Information is to be passed down the chain of production, with producers and importers obliged to provide this information on to everybody who uses chemicals in their production processes.

REACH also applies to certain chemicals in products if they are in concentrations greater than 0.1% by weight of the product or if they are intended to be released from the article. (Products are called articles in REACH terminology.)

Our sustainability and supply management teams will continue to work to align for next steps in the implementation of REACH.

GHS

The Globally Harmonized System of Classification and Labeling of Chemicals (GHS) is a United Nations system to identify hazardous chemicals and to inform users about these hazards through standard symbols and phrases on the packaging labels and through safety data sheets. In 2007 the European Commission adopted a proposal to implement the GHS in Community law through a regulation on classification, labeling and packaging of substances and mixtures. This will contribute to internationally harmonized communication of hazard information on chemicals and facilitation of trade.

The proposed regulation will complement REACH. It will also adapt certain provisions of REACH relating to classification and labeling.

As of year-end 2007 the proposal was undergoing the legislative co-decision procedure, seeking agreement of the European Parliament and the Council.

Take-back and recycling

Dealing with electronic waste is a concern for industry and society. E-scrap is one of the fastest growing components of the global waste stream.

At Philips we incorporate design-for-recycling into our overall EcoDesign process. This is critical to reduce the cost of recycling a product at the end of its useful life, because the cost of taking apart many consumer electronics can be higher than the value of the materials. Designers must balance this with keeping other environmental issues under control, including materials use and energy consumption.

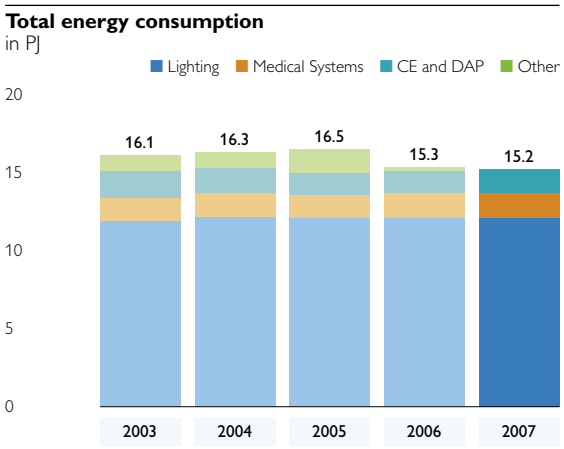
WEEE

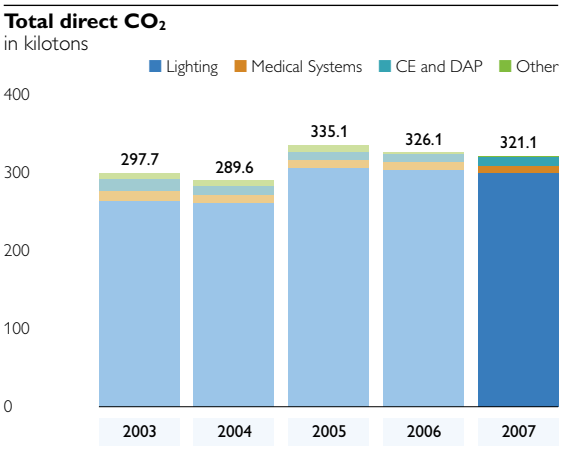
The EU Directive on waste electrical and electronic equipment (WEEE) makes producers responsible for taking back and recycling electrical and electronic equipment.

Legislation related to WEEE varies by country and some have not yet put legal requirements in place. This makes implementation complex.

The WEEE legislation has accelerated the adoption of end-of-life product take-back regulations around the world. In the United States, for example, electronics recycling bills were introduced in 23 states in 2007.

We were at the forefront in the mid-1990s when we initiated a project called "Apparatour," aimed at developing a complete understanding of the recycling possibilities of WEEE. In cooperation with the local authorities in Eindhoven, the Netherlands, and a substantial number of villages around the city, the project included investigating costs, logistics and the applicability of disassembly techniques. Disassembly was tested at the recycling company Mirec, a Philips subsidiary at that time. (Today Mirec is part of the Australian-headquartered Sims Group, a multinational company providing recycling solutions.)





Taking "steps" to solve the e-waste problem

Philips is a charter member of the global public-private initiative called Solving the E-Waste Problem (StEP). Officially launched on March 7, 2007, StEP charter members include Hewlett-Packard, Microsoft, Dell, Ericsson, and Cisco Systems, along with UN, governmental, non-governmental and academic institutions, as well as recycling/refurbishing companies.

Prime goals of the initiative are to standardize recycling processes globally to harvest valuable components in electrical and electronic scrap (e-scrap), extend the life of products and markets for their reuse, and harmonize world legislative and policy approaches to e-scrap. A global guide to dismantling e-scrap and maximizing the recovery and controlling recovered substances is a major StEP objective.

Inter-related StEP task forces will help shape government policies worldwide and address issues related to re-design and product life expectancy, re-use and recycling, and help build relevant capacity in developing nations.

EcoVision III (2006-2009)

Our EcoVision III environmental action program began in 2006 and will run through 2009. In developing this program, societal relevance provided the foundation for a focus on the environmental issues stated earlier – energy efficiency, chemical content of products, and take-back and recycling – which are Green Focal Areas for product development. Further, we are continuing to work on optimizing our processes, striving to significantly reduce or eliminate emissions of the hazardous substances discussed in the following pages.

Products

Our EcoDesign process, introduced in 1994, deals with all phases of product development. With our first EcoVision program in 1998, we introduced the Green Flagship concept. To drive a disciplined, rigorous approach to EcoDesign, only our top EcoDesigned products achieved Green Flagship status after undergoing a benchmark analysis.

As more technologies and even complete product ranges could be identified as "green," particularly in Philips Lighting, we broadened our definition to "Green Products" in 2007.

We also launched our latest environmental action program, EcoVision4, in 2007. With this program we have committed, among other things, to generate 30% of total revenues from Green Products over the next five years (up from 15% in 2006).

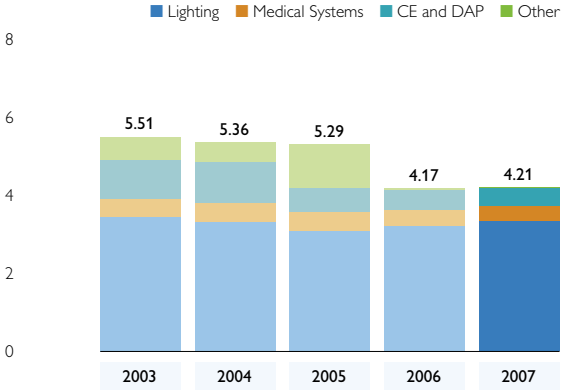
Philips Green Products offer customers, users and society a significant environmental improvement in one or more of the Philips Green Focal Areas:

To support our DoseWise Radiation Safety program at every level of new product design and development, we have expanded in 2007 the definition of the Green Focal Area hazardous substances to include this important topic.

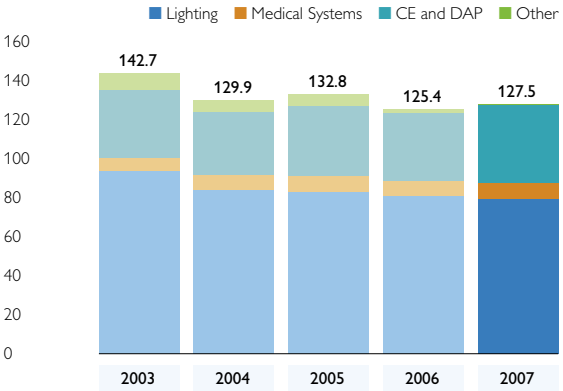
We use the Life Cycle approach to determine a product's overall environmental improvement. The Life Cycle Assessment calculates the environmental impact of a product over its total life cycle (raw materials, manufacturing, product use and disposal). The result of such a calculation is an Eco-Indicator.

The score for a given product in a Green Focal Area is significantly better when it is 10% better than

Total water intake
in million m³



Total waste
in kilotons



the reference product, which can be a competitor, predecessor or other product in the particular product family.

2007 saw sales of Green Products increase to 20% of total sales, compared with 15% in 2006, representing an important part of our revenue stream.

Processes

Energy

Absolute energy use is stable at 15,214 TJ in 2007. Taking into account a production decrease of 2%, in relative terms the company used 1% more energy due to production mix changes mainly in Lighting and CE.

Direct CO_2 emissions

We are reporting 321 kilotons of direct CO_2 emissions in 2007 from manufacturing, compared to 326 kilotons in 2006, mainly resulting from use of natural gas for heating systems. This 2% decrease is related to mild weather conditions. For the total CO_2 equivalent emissions, please see details on the Philips operational carbon footprint on page 25.

PFC emissions contribute to global warming and are expressed in CO_2 equivalents. These are emitted at two Medical Systems sites, at the level of 34 kilotons CO_2 equivalents in 2007, compared to 32 kilotons CO_2 equivalents in 2006. This is attributable to a 43% production increase.

The use of air-conditioning refrigerants and the use of CFCs and HCFCs in manufacturing result in emissions that contribute to global warming. Expressed in CO_2 equivalents, emissions in 2007 were 5.4 kilotons, compared with 6.1 kilotons in 2006.

Water

Water is used primarily for domestic purposes. However, in the Lighting sector water is also used in production, accounting for 80% of total water use.

In absolute terms, water usage increased to 4.21 million m³ in 2007 from 4.17 million m³ in 2006, representing a 1% increase. While production decreased approximately 2% companywide, demand for cooling capacity increased due to additional production equipment at Lighting. In 2007, the ratio of purchased water to that we extract was approximately 3:2.

Waste

Total waste increased from 125.4 kilotons in 2006 to 127.5 kilotons in 2007. Lighting (62%) and CE (25%) share 87% of our worldwide total waste. CE accounted for a slight increase, due to rising packaging waste from overseas contractors combined with a changeover to larger TV panel sizes.

Total waste is made up of actual waste delivered for either landfill or incineration, comprising 17% non-hazardous and 4% hazardous waste, and recyclable waste. Materials delivered for recycling via an external contractor comprised 100 kilotons or 79% of total waste.

Restricted substances: benzene

Lighting is the only sector that uses benzene in manufacturing. During the course of 2007, 52 kg of benzene, as a by-product in carriers for lacquers, was reported, compared with 6 kg in 2006. An elimination program was initiated and the substance was phased out by year-end.

Restricted substances: mercury

Mercury is used exclusively by Lighting in production. The setting up of mercury balance sheets in 2006 has lead to a substantial decrease of reported mercury emitted, from 197 kg in 2006 to 185 kg in 2007.

Restricted substances: CFCs/HCFCs

In 2006 the total emissions from CFCs/HCFs was 160 kg, mainly in Medical Systems. In 2007 this increased to 202 kg, the result of a one-time event due to the repair of the cooling system at a DAP site.

Other restricted substances

Emissions of other restricted substances totaled 0.9 tons, largely attributable to Medical Systems and Lighting, down from 1.7 tons in 2006. This decrease is due to a change in processes and related equipment, as well as lower production volume.

Hazardous substances: lead

In 2007 a total of 3.9 tons of lead emissions were reported, a decrease of 8% compared to 2006. Lead is mainly used in soldering at Lighting facilities outside of Europe. In keeping with our EcoVision target to reduce the use of lead in our processes, elimination programs are underway.

Hazardous substances: toluene

Toluene emissions dropped 51% in 2007 to 1.4 tons from 2.8 tons in 2006. The Lighting sector partially eliminated the use of toluene in production.

Hazardous substances: xylene

92% of the 2007 total xylene consumption was reported by Lighting, with DAP accounting for 7%. The total amount reported is 4.5 tons in 2007, an increase of 2% compared to 2006. This is attributable to a change in product mix in Lighting. In view of the EcoVision targets, elimination programs are in place.

Other hazardous substances

The total of other hazardous substances (including antimony, specific chlorinated/brominated organic compounds and styrene) reported in 2007 is 151 tons, compared with 106 tons in 2006. 99% of this total is attributable to Lighting in the form of styrene. Styrene moved from the category relevant substances to the category hazardous substances in 2006.

ISO certification

Company policy requires that all manufacturing sites achieve ISO 14001 certification. The company also recommends that non-industrial facilities obtain certification. At year-end 2007, 90% of our industrial reporting organizations were ISO 14001 certified.

Legal compliance

Compliance issues are resolved through local management with legal counsel. For information about provisions for environmental remediation please refer to the *Philips Annual Report 2007*.

Incidents

In 2007, 15 incidents were reported in five categories. They were related to waste (two), water (six), soil (one), and emissions of relevant substances (three) and fire (three).

Our economic performance

In 2007 we continued to advance well in our drive to become a truly market-focused, people-centric company that is geared to creating value through sustained profitable growth. Operationally, we delivered once again on our Group targets, with 5% comparable sales growth and an EBITA margin of 7.7%, thanks to good execution, a strong innovation pipeline and a balanced portfolio that proved its robustness in a weakening economic environment.

Economic stakeholders

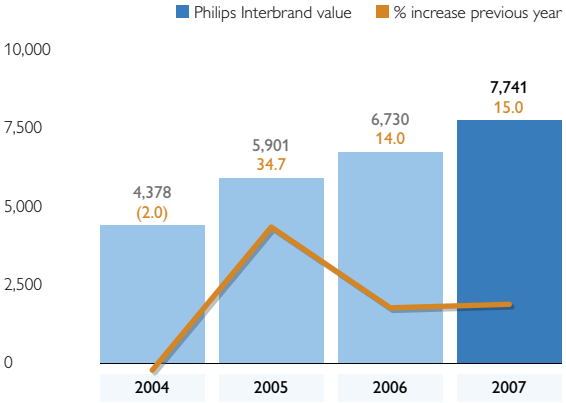
Many stakeholders have a direct or indirect economic interest in our company's performance. Direct economic impacts are often measured as the value of transactions between the reporting organization, the Philips company and its stakeholders. Customers, suppliers and employees are clearly main groups in terms of direct transactions.

Indirect impacts are important to assess in relation to local communities and regional economies. These indirect economic impacts can provide an indication of where reputational risks may develop, or where opportunities may emerge to expand market access or a social license to operate. In this report, however, we limit the scope to direct economic impacts on a global level, representing the company as a whole.

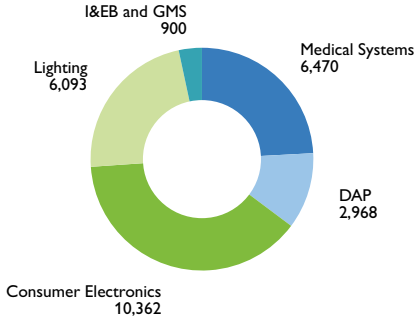
Customers

Loyal and satisfied customers are the longer-term lifeline for any company. Strategically, we made significant steps in building strong market leadership positions across the portfolio, by investing in high-growth high-margin businesses while continuing to divest some low-growth low-margin businesses, largely completing our portfolio transformation. In particular, the announced acquisitions of Genlyte and Respironics will boost our leadership position in Lighting and Home Healthcare respectively.

Brand value
in millions of US dollars



Sales by sector 2007
in millions of euros



Brand value

In 2007, we continued to invest in building the Philips brand, supported by the EUR 111 million investment in the global brand campaign. These efforts resulted in a substantial increase in our brand value as reported by Interbrand. Philips' brand value increased by 15%, to USD 7.7 billion from USD 6.7 billion. The Philips brand was ranked the 42nd most valuable global brand in 2007, up from the 48th in 2006.

This development is primarily driven by increased appreciation of our Medical Systems businesses, which currently represent the highest brand value within the group. The Interbrand analysis showed that 35% of sales decisions in the healthcare sector are made based on brand. This demonstrates the importance of a strong brand for driving sales in the business-to-business as well as the business-to-consumer environment. The Philips brand is strongly positioned to do so.

Sales of the Philips Group

We delivered on our growth target, realizing 5% comparable sales growth, despite unfavorable currency movements. Our strong innovation pipeline and balanced portfolio proved their robustness in a weakening economic environment. Growth was realized by all divisions, with DAP (15%) and Lighting (6%) delivering particularly strong growth. With market share losses and an increasingly competitive market environment for Consumer Electronics in 2007, especially Connected Displays in the United States, comparable sales growth at CE was limited to 1%. At Medical Systems, comparable sales increased by 4%, despite a softening of the imaging market in the United States, due in part to the impact of the Deficit Reduction Act, and in Japan.

Geographic sales distribution

We monitor our performance on a geographical axis based on the following market clusters:

- key emerging markets, including China, India and Latin America
- other emerging markets, including emerging markets in Central and Eastern Europe, Russia, Ukraine and Central Asia, the Middle East and Africa, Turkey and the ASEAN zone
- mature markets, including Western Europe, North America, Japan, Australia and New Zealand.

In 2007, sales growth was particularly strong in emerging markets, which will continue to be a focal area of growth for Philips. Emerging markets, most notably China, Russia and India, contributed 60% to our comparable sales increase in value, while accounting for approximately one third of total revenues.

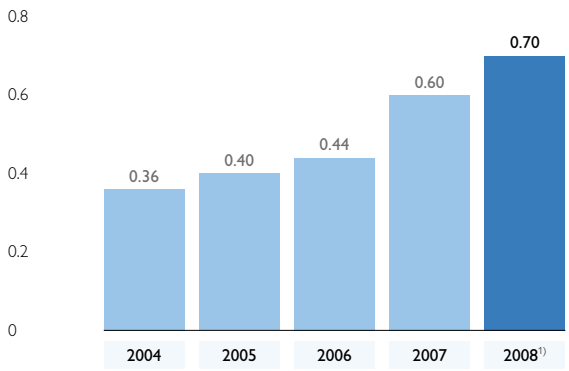
Key emerging markets showed strong comparable growth, primarily driven by Lighting, Medical Systems and DAP, partly offset by a sales decline at CE, mainly due to Connected Displays in Latin America. Other emerging markets delivered strong double-digit sales growth compared to 2006, driven by the outstanding performance of DAP and CE as well as robust expansion of Lighting and Medical Systems in these countries.

Sales in Western Europe showed a solid increase on a comparable basis, visible in all sectors. In North America, sales on a comparable basis remained stable compared to 2006. A strong performance by DAP, driven by the successful introduction of new shaving and oral healthcare products, and moderate growth at Medical Systems, despite a decline at Imaging Systems, were largely offset by lower comparable sales at CE, predominantly attributable to strong competition and price pressure in FlatTV.

Suppliers

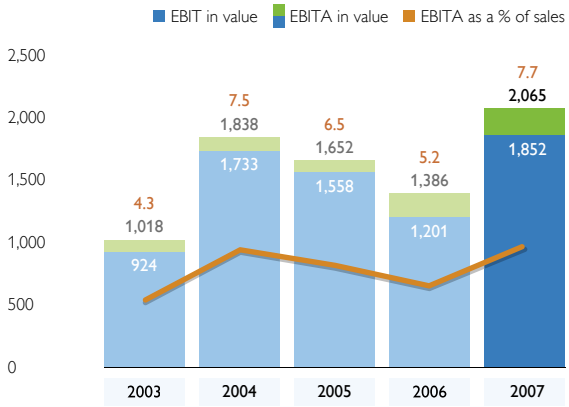
Total products and services purchased in 2007 amounted to EUR 19.2 billion, representing 72% of total sales.

Dividend per common share
in euros



[1)] Subject to approval by the 2008 Annual General Meeting of Shareholders

EBIT and EBITA
in millions of euros



2007 marks the fourth year of a comprehensive change program. Supply Management plays a key role in value creation, and 77% of Philips' spend is now centralized or center-led. From 2003 until 2007 the total number of active suppliers was reduced from more than 50,000 to less than 20,000.

80% of spend on Bill of Material is now concentrated on fewer than 300 suppliers, and in non-product related on less than 800 suppliers world wide. This drive plays a strategic role in value creation for our company and stimulates suppliers to be strategic partners for the future. Further details on supply spend are included in the section on "Our suppliers."

Employees

Wages

The composition of our workforce and the changes in 2007 are addressed on page 72. The total wage bill in 2007 was EUR 3,904 million, compared with 4,612 million in 2006. Salaries and wages include an amount of EUR 35 million (2006: EUR 78 million) relating to restructuring charges.

Pensions

In 2007, net periodic pension costs of defined-benefit pension plans amounted to EUR 27 million, compared with EUR 75 million in 2006, mainly due to an increase in plan assets in 2006. The payments to defined-contribution pension plans amounted to EUR 84 million, EUR 4 million higher than in 2006, largely due to acquisitions.

Providers of capital

Interest income in 2007 was EUR 236 million, an increase of EUR 86 million compared to 2006, mainly as a result of higher average cash balances and higher average interest rates. Interest expense was EUR 279 million, a decrease of EUR 60 million from 2006, mainly as a result of lower average debt positions and lower interest costs on derivatives related to hedging of Philips foreign currency denominated cash balances and inter-company funding positions.

The net interest expense in 2007 was EUR 43 million, a decrease of EUR 146 million compared to 2006.

Shareholders

Economic benefits for the shareholders include several aspects. The direct impact relates to payments of dividends, totaling EUR 639 million in 2007, or EUR 0.60 per common share. It is proposed to increase the dividend for 2007 by 17% to EUR 0.70 per common share.

Another direct effect came from the repurchasing program of shares. During the year 2007, we repurchased EUR 1.6 million of our shares. Following an amendment to Dutch tax legislation, we announced of further EUR 5 billion (tax-free) share repurchase plan.

Governments

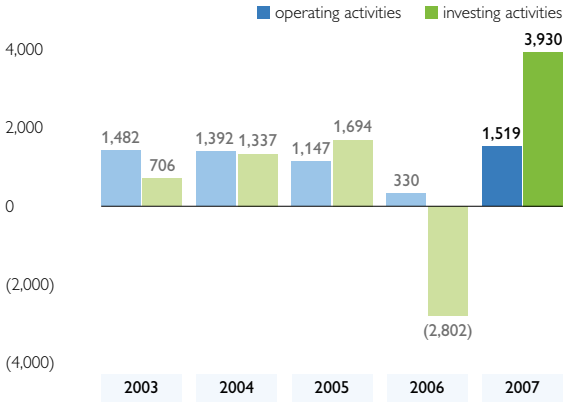
Income taxes amounted to EUR 622 million, compared to EUR 167 million in 2006. The tax burden in 2007 corresponded to an effective tax rate of 13.9% on pre-tax income, compared to 13.6% in 2006. The effective tax rate in 2007 was affected by tax-exempt items such as the non-taxable gain on the sale of shares in TSMC, the market-value adjustment of JDS Uniphase and the fair-value adjustment of TSMC shares and the TPV convertible bond. For 2008, the effective tax rate excluding non-taxable items is expected to be around 30%, broadly in line with 2007.

Financial performance in 2007

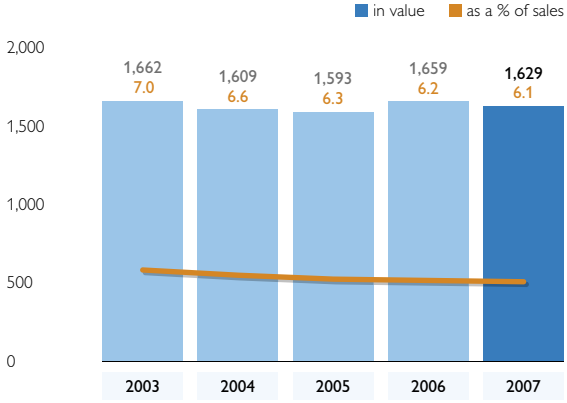
For a full understanding of the company's financial performance in 2007, please refer to the *Philips Annual Report 2007*.

In 2007, our gross margin of EUR 9,169 million, or 34.2% of sales, improved by EUR 919 million compared

Cash flows from operating and investing activities
in millions of euros



Research and development expenditures [1)]
in millions of euros



[1)] Restated to present the MedQuist business as a discontinued operation

to 2006 (EUR 8,250 million, or 30.9%). Adjusted for the asbestos-related product liability charge in 2006 (EUR 256 million), gross margin improved from 31.9% of sales to 34.2%. This improvement was primarily driven by higher gross margins at Medical Systems and Lighting.

In 2007, EBIT increased by EUR 651 million compared to 2006, to EUR 1,852 million or 6.9% of sales. Excluding the EUR 256 million asbestos-related product liability charge which was recognized in 2006, EBIT profitability improved by 1.4% in relation to sales, driven by the improved performance of DAP, Lighting and Group Management & Services.

Total EBITA for the Group increased from EUR 1,386 million, or 5.2% of sales, in 2006 to EUR 2,065 million, or 7.7% of sales in 2007, exceeding the Group's profitability target of 7.5%. The main drivers of the year-on-year EBITA improvement were the strong, mainly sales-driven performance at DAP (EUR 145 million) and higher earnings at Lighting (EUR 114 million), as a result of higher sales across almost all businesses and a lower loss in the fluorescent-based LCD Backlighting business. Excluding the EUR 256 million negative impact of product liability charges in 2006, Group Management & Services' result improved by EUR 146 million due to reduced corporate and regional costs as well as lower pension and brand campaign costs.

Net income from continuing operations amounted to EUR 4,601 million, an increase of EUR 3,700 million compared to 2006. The improvement was driven by EUR 651 million higher operational earnings and EUR 2,585 million increased financial income, primarily due to the sales of shares of TSMC.

Cash flows from operating activities increased to EUR 1,519 million in 2007, up from EUR 330 million in 2006, mainly due to higher operating results in 2007 and accelerated pension contributions in the United Kingdom and the United States.

Research & development

Strong performance in innovation is critical for Philips to maintain and increase its market competitiveness. Through substantial investments in research & development (R&D), Philips has created a vast knowledge base.

The Chief Technology Officer (CTO) of Philips manages the enabling technologies across the company. Corporate Technologies, employing 2,800 people, invests in world-class competencies and technologies that are relevant to the entire Philips Group. In the operating divisions, some 7,800 employees in 26 countries are predominantly engaged in the development of products and applications.

In 2007, we invested EUR 1.6 billion, or 6.1% of sales, in research & development, slightly less than in 2006. Higher investments in Medical Systems, Lighting, DAP and Innovation & Emerging Businesses were more than offset by lower expenditures in CE, largely due to the divestment of Mobile Phones.

Our suppliers

The Company's mission for supply management is to create value by extracting the power of One Philips and transforming the transactional purchasing function into strategic supply management.

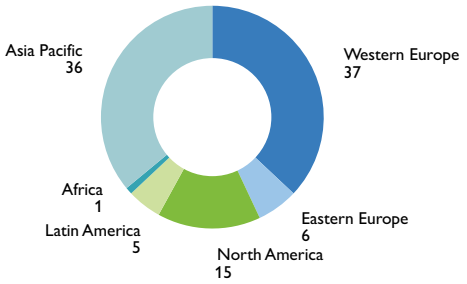
2007 marks the fourth year of a comprehensive change program. Supply Management plays a key role in value creation, and 77% of Philips' spend is now centralized or center-led. From 2003 until 2007 the total number of active suppliers was reduced from more than 50,000 to less than 20,000. 80% of spend on Bill of Material (BOM) is now concentrated on fewer than 300 suppliers, and in Non-Product-Related (NPR) on less than 800 suppliers world wide.

Extracting the power of One Philips

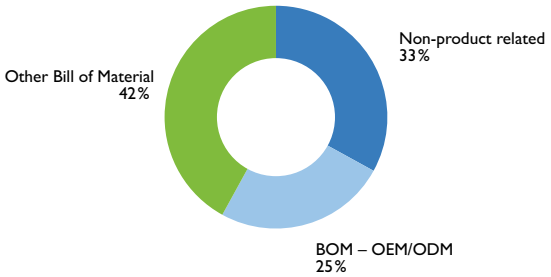
Leveraging the company's spend and resources in key areas and negotiating as One Philips improves time-to-market, reduces total cost of ownership and increases quality. Strategic priorities are:

- NPR spend: Philips has centralized its NPR spend management in Philips General Purchasing. In addition to enhancing negotiating power, this organization initiates cost-savings projects together with operational units and suppliers, in the areas of cost avoidance and efficiency enhancement. During 2007 the transactional shared service centers for NPR purchasing were outsourced, together with the finance shared service activities, to Infosys.
- Cross-sector BOM opportunities: ownership of some EUR 3 billion cross-sector spend is concentrated centrally. Cross-sector teams led by sector Chief Purchasing Officers are active in 10 commodity areas, including metals and electronic components. Centralized One Philips leveraging of this spend with fewer, more strategic suppliers has resulted in significant value creation.
- Outsourcing strategy and guidance: this initiative supports industrial strategy decision-making, addressing the shift in resources required to manage

Total purchased products and services in 2007, by geographic area
as a % of total



Total purchased products and services in 2007, by type
as a % of total



the change to an outsourcing relationship. Our total OEM/ODM (Original Equipment Manufacturer/ Original Development Manufacturer) outsourcing spend has almost doubled in the past three years to EUR 6.5 billion. To encourage development of more strategic relationships, the number of preferred EMS (Electronic Manufacturing Systems) suppliers has been reduced from 61 in 2004 to eight in 2007.

Supply Management has set an ambition in 2005 to achieve two-year cumulative savings of EUR 1 billion in the One Philips spend categories. This target was met in the 2006/2007 timeframe and has helped to maintain and improve the competitiveness of the company.

One Philips approach to supplier sustainability

Since we introduced our Supplier Sustainability Involvement Program in 2003, we have made considerable progress. We have improved transparency in our supply chain and reporting, strengthened our internal monitoring systems and have been embedding sustainability into our supply management processes.

Given the importance of this topic, sustainability is now a routine agenda item at our monthly business review meetings, including continuous monitoring of corrective action implementation. Achieving a sustainable supply base is an ongoing process that needs execution at all levels of the company.

We firmly believe that this is a matter of taking care of the environment and of workers' lives. As a member company of the Electronic Industry Code of Conduct (EICC) we share the organization's goal to improve conditions in the electronics supply chain. The EICC member companies are "collaborating to help ensure safe conditions, worker rights and environmental responsibility in the global electronics supply chain."

Supplier sustainability governance

Based on our governance model, each sector is responsible for the compliance of its supply base.

A Senior Vice President, Supplier Development and Sustainability, is responsible for continuing to embed sustainability throughout the supply chain. This position reports to the Chief Procurement Officer, who is a member of the Philips Group Management Committee and Chair of both the Supply Management Leadership Board and the Sustainability Board.

The Supply Management Leadership Board is responsible for program deployment and consists of the CPOs of each sector. Our Supply Sustainability Platform is comprised of Supply Sustainability Officers from each sector and Philips General Purchasing, plus representatives from Corporate Legal, Corporate Sustainability Office and Internal Audit. Chaired by the Senior Vice President, this group leads our overall supplier sustainability program. Our supply managers are obligated to select suppliers that act with integrity and are in compliance with applicable laws and the Philips Supplier Sustainability Declaration, as laid out in the Philips General Business Principles and Supply Management Code of Ethics. Each sector's CPO must approve new suppliers after assessing, among other things, the critical competencies and the sustainability status of the proposed supplier.

Lead buyers play a pivotal role. They are responsible for communicating requirements to suppliers, requesting and scheduling audits, ensuring audits are executed and that corrective actions are implemented. If necessary, the CPOs support the lead buyers as they work with suppliers to facilitate changes in a supplier's operations. In some instances issues are escalated to the CEO of the sector.

Toward standardization

We endorsed the Electronic Industry Code of Conduct (EICC) in 2006 and joined its Implementation Steering Committee. Working with EICC member companies to develop standardized tools and processes, allows for increased efficiency, productivity and simplicity for our suppliers and ourselves. It's a practical example of delivering on our brand promise, "sense and simplicity."

Reflecting our drive for consistency, we updated our Philips Supplier Sustainability Declaration in 2006 to align with the EICC standards. To safeguard the level of standard set, we have included an appendix elaborating further on employees rights related to freedom of association/collective bargaining. This is in keeping with our original Supplier Sustainability Declaration. Where freedom of association/collective bargaining is restricted by law, we look to see if there are other means of open communication between the supplier's management and workers.

During 2007 we participated in the EICC quarterly meetings and in many working groups, conducted sessions with non-governmental organizations and teamed up other companies to drive standardization and ensure a level playing field for our sector.

Supplier Sustainability Program approach

The Philips Supplier Sustainability Program is built on the following pillars:

- Setting out our requirements
- Building understanding and agreement
- Monitoring suppliers
- Resolving issues
- Stakeholder engagement.

To determine where to focus our efforts, we have developed an approach based on a risk profile related to spend, country of production, business risk and type of supplier relationship.

Setting out our requirements

When we launched our Supplier Sustainability Involvement Program in 2003, a first step was to raise awareness among our suppliers through training. This led to the request for adherence to the Philips Supplier Declaration on Sustainability, which outlines our expectations of behavior in the areas of environment, health and safety, and labor conditions. Our Supplier Sustainability Declaration applies to our suppliers with a spend above EUR 1,000.

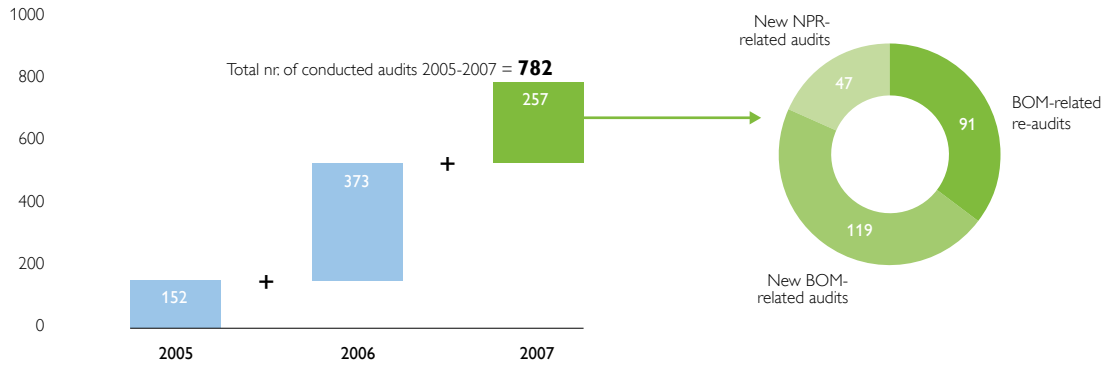
In 2007 we implemented our updated Declaration, which is being signed by all of our suppliers. The new Declaration is included in our updated Purchase Agreements.

The Royal Philips Electronics List of Restricted Substances is also part of our Purchase Agreements. The list specifies those substances that are not allowed in products above our established threshold to ensure that all products put on the market do not contain substances restricted by law and regulations, including RoHS (the European Union Directive on the restriction of the use of certain hazardous substances in electrical and electronic equipment).

Our Healthcare sector includes the Royal Philips Electronics List of Relevant Substances in its Purchase Agreements and Consumer Lifestyle does so as appropriate. This is a list is of substances to which we pay attention from a precautionary point of view.

The principle states that in order to protect the environment, a precautionary approach should be widely applied, meaning that where there are threats of serious or irreversible damage to the environment and/or health, lack of full scientific certainty should not be used as a reason for postponing cost-effective preventive measures. Simply put, our philosophy is that "prevention is better than cure."

Total Philips supplier sustainability audits



	2005	2006	2007
BOM-related audits	150	365	210
NPR-related audits	2	8	47

Building understanding and agreement

We work with our suppliers to raise awareness about the importance of operating in a sustainable manner and provide guidance on how to do so. Our sectors conduct training sessions, supplier day events or specific briefings. Regardless of the venue, suppliers are encouraged to share their experience.

As an integral part of how we do business, sustainability was an important agenda item at our briefings with suppliers. In 2007 Consumer Electronics organized meetings in Shenzhen and Shanghai for a total of 160 suppliers, while Lighting hosted 60 suppliers in Shanghai. At nine DAP supply centers around the world invited key suppliers (typically 20) to attend briefings on sustainability.

We also continued to conduct training on the Philips Supplier Sustainability Program for our employees in 2007, including internal auditors, HR, Quality, site management, business groups and purchasers. Training was held at Philips sites around the world, including China, Singapore and the Netherlands. In December we focused on the change of our audit checklist to that of the EICC, when it is finalized. By February 2008 all lead auditors will have attended this refresher course.

Our suppliers are advised to do the self-assessment and we make clear our audit checklist. They are required to sign the Supplier Sustainability Declaration to testify their commitment and identified risk suppliers are required to pass our sustainability audit. The audit checklist divided issues into zero-tolerance, limited tolerance and minor. Zero-tolerance issues are, for example: child labor, continual seven-day work weeks, immediate life threatening situations, slave labor conditions and banned substance found in the supplier supply chain.

Monitoring suppliers

Our supplier self-assessment tool and audits have been used to enable our sectors to monitor compliance with our requirements throughout our supply base.

Self-assessment tool

If the perceived risk goes above a certain level, suppliers are asked to perform a self-assessment. This further builds awareness, giving suppliers the opportunity to resolve issues internally. This tool is used as part of our control structure. While we had planned to eliminate this for a specific category of identified risk suppliers, all self assessments done revealed the need for audits to take place.

Sustainability audit approach

For 2007 we set a target to achieve full transparency by auditing 100% of our identified risk supplier sites. This gives us a clear picture of the sustainability risks we may be facing with those suppliers. (Since then we have been auditing all potential suppliers that are identified as risk suppliers.)

To help us determine our criteria, we identified risk countries based on independent sources and also determined a threshold based on spend. As a result, suppliers who provide us with goods and services from manufacturing sites in Brazil, China, India, Indonesia, Mexico, Pakistan, the Philippines, Thailand and Vietnam, and with whom we also spend more than EUR 100,000, were identified as risk suppliers. In addition, if suppliers are identified as risk suppliers outside this scope, they are also audited. Likewise, as mentioned above, all potential suppliers that are identified as risk suppliers automatically undergo audits as part of the supplier selection and approval process.

Our 2007 audits were conducted by internal Philips auditors and by the external auditor, SGS Group. Going forward, the use of external auditors will

increase, allowing our internal resources to focus on resolving issues, as well as initiating CO_2 reduction projects with our suppliers and full supplier certification.

During 2007 all auditors used the Philips audit tool, which has been aligned with the EICC where possible on chapters Labor, Health & Safety, Environment and Management Systems. The current beta version of the EICC audit tool is supporting us in our efforts to strengthen the scope and depths of our audits. In the spirit of continuous improvement, we have been fine-tuning the audit process and are working with the EICC to enhance the beta version of the audit tool, which we will deploy when the final version is released.

The quality of the auditing process is maintained through the review of each audit report. Periodic review of the audit program with SGS includes a Philips specialist joining an audit as an observer and asking suppliers about the service received. In addition, individual SGS auditors are asked about their audit experience. As is the case with any form of outsourcing, maintaining expertise and control the overall process is paramount.

We are building experience with the periodic double checking of deliveries regarding banned substances. The check is carried out by supplier quality control personnel and if issues are found they are escalated to sustainability officers and other responsible persons. A thorough check of the related processes at the site is then started.

Resolving issues

We take non-compliances seriously and continuously monitor and support the implementation of corrective actions at our suppliers' manufacturing sites. In order to manage issues identified during an audit, we have categorized non-compliances into zero-tolerance, limited-tolerance (formerly referred to as major).

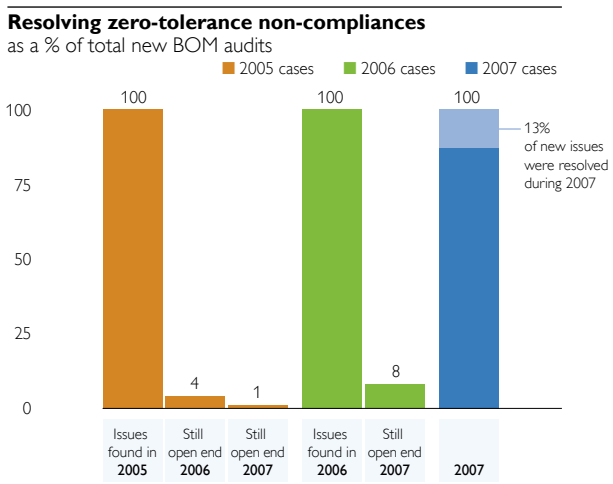
This categorization determines both the appropriate timeline in which the supplier should complete corrective action and what internal escalation procedures we need to take if issues are not being adequately addressed by the supplier. Timelines are defined by severity or time needed to resolve the issue. For example, health and safety issues can be resolved relatively quickly with considerable positive impact on the employees involved.

After audits, the lead buyer works with suppliers to ensure that the supplier acts upon the required corrective action in the agreed timeline. In general, we prefer to resolve issues at operational level whenever possible, further embedding sustainability into the purchasing function. The implementation of solutions is monitored at regular meetings with suppliers.

The resolution of zero-tolerance and limited-tolerance non-compliance issues is monitored internally using a cross-sector escalation process.

This process of monitoring issues resolution involves sector CPOs and business management, and is needed if business interests are vulnerable, including issues with single-source suppliers where we have few or no alternatives. Our sector General Business Principles (GBP) compliance officers are involved in monitoring this reporting process and internal audit has added the topic to its overall risk assessment with the sectors. A report of all issues and their resolution is also an integral part of the GBP non-compliance reporting.

If a supplier does not make progress in implementing corrective actions, or if they continue to use unacceptable practices, we will end our relationship with them as a last resort. This decision may have an impact on our business and if so we carefully prepare a contingency plan.



Closing issues identified during 2006 audits

At the end of 2006 we had audited 98% of our suppliers. The issues found were described in the *Philips Sustainability Report 2006*.

During the course of 2007 we resolved 92% of the remaining zero-tolerance issues identified during our 2006 audits. That included monitoring to verify whether corrective actions had been properly implemented. However progress on resolution, specifically in closing zero-tolerance issues, was slower than expected.

The most frequent sustainability non-compliances identified in 2006 were in the areas of working hours, emergency preparedness, occupational safety, and environmental management systems.

Looking at specific findings, non-compliances associated with working hours were most common in China and Thailand. This is frequently related to overtime not conforming to legal limits or where employees routinely work seven-day work weeks. Possible solutions are set out on page 99.

As the supplier's customer, we work with our customers to optimize demand management to avoid unanticipated spikes in production.

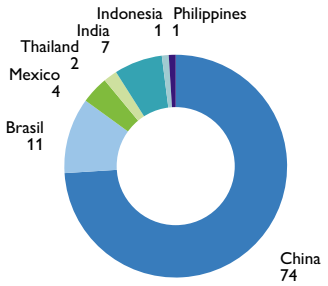
Emergency preparedness was found lacking at many supplier sites. We noted unawareness about the need to have fire safety procedures and measures in place. The same applies for the use of personal protective equipment, which is the main finding in the area of occupational safety. These issues have been relatively easy and quick to resolve. It's a matter of raising awareness and providing basic safety measures like fire-prevention and signage to identify escape routes.

With respect to pollution prevention and resource reduction, the most frequently seen non-compliance was the absence of environmental management systems (EMS) at the sites audited. We support suppliers with links to experts to support projects to implement such systems, but this is something that takes time. Implementing an EMS typically takes 9-15 months and we follow the suppliers' progress until fully certified.

In terms of humane treatment, the main non-compliances found were of suppliers that did not have policies or procedures against harassment or describing disciplinary measures, and have been solved.

We have learned that it often took longer to resolve issues that we had anticipated. When we began our Supplier Sustainability Involvement Program in 2003, we set ambitious targets for ourselves. Experience has proven that some issues could not be resolved in the aggressive timetable we established. However, now that most of the zero-tolerance issues identified in our 2006 audits have been resolved, and we are continuing to monitor the changes that have been implemented, we have gained the necessary experience to handle issues in a shorter timeframe.

Distribution of identified risk supplier audits, 2007
as a % of total BOM-related audits in risk countries



Summary supplier sustainability BOM-related audit results 2007

% of new audited BOM sites in risk countries where the following types of non-compliance were found

	Zero tolerance	Limited tolerance
Labor		
Freely Chosen Employment		15<25%
Child labor avoidance	<5%	5<15%
Working hours	25<50%	>50%
Wages & benefits		>50%
Humane Treatment	<5%	5<15%
Non-discrimination		<5%
Freedom of association		
Collective Bargaining		
Health and safety		
Occupational Safety	25<50%	25<50%
Emergency Preparedness		25<50%
Occupational Injury and Illness		
Industrial Hygiene		5<15%
Dormitory and canteen		
Environmental		
Environmental permits and reporting		15<25%
Pollution prevention and resource reduction		25<50%
Hazardous substances	<5%	5<15%
Product content restrictions		15<25%
Management system		
Company Commitment	<5%	
Legal and customer requirements	<5%	

● <5% ● 5<15% ● 15<25% ● 25<50% ● >50%

Overview of 2007 audit results

We extended our audit approach to include NPR in 2007. We completed 257 sustainability audits of identified risk supplier sites, achieving our target of 100% transparency. Of that total, 210 were BOM-related and 47 were NPR-related.

New suppliers accounted for 57% of BOM-related audits, while 43% were audits of BOM suppliers with open issues from the 2006 audits.

Suppliers of new ventures are included to the extent that the integration process has been finalized, during the transition process and divestments are included until purchasing responsibility ends.

All took place at supplier sites with a spend above EUR 100,000, in Brazil, China, India, Indonesia, Mexico, the Philippines and Thailand. This includes some strategic second-tier identified risk supplier sites (those we selected for our first-tier suppliers). SGS Group conducted 159 audits, or two-thirds of all audits, an increase of one-third compared with 2006.

The table provides a summary of the zero-tolerance and limited-tolerance non-compliances found during BOM audits. Minor non-compliances are handled at sector level and are no longer reported into our central database.

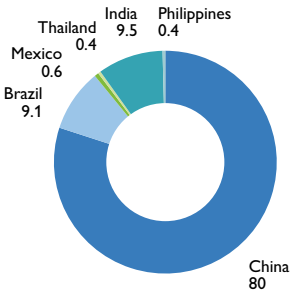
Bill of Material supplier audit results

Compared with 2006, we found a higher number of limited-tolerance non-compliances per audit held, possibly due to the experience gained by our internal and external auditors.

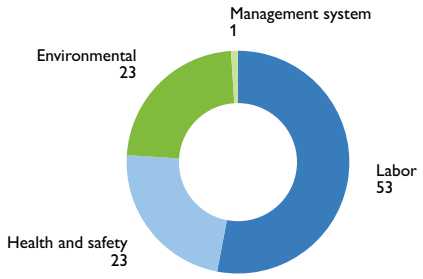
Roughly half of the non-compliances were due to labor issues, with a quarter due to health and safety and the remaining quarter due to environmental issues.

The most frequent labor issue continues to be related to working hours. This is clearly a fundamental issue, and we believe that cooperation with the EICC and local governments is the only way to truly achieve sustainable change. A first example is a project established in Dongguan, China, that brings together local government, entrepreneurs and labor representatives to build a program to ensure compliance to local law.

Distribution of non-compliances by country, 2007
as a % of total BOM-related audits in risk countries



Distribution of non-compliances by grouping, 2007
as a % of total BOM-related audits in risk countries



This project was carefully constructed as a multi-stakeholder initiative to be supported by the government, civil society, industry associations and customers. The partners that are working on this project include FIAS (World Bank Group), Business for Social Responsibility, Shenzhen Electronics Industries Association, the EICC and the Global eSustainability Initiative. Additionally, research and input were provided by a wider set of stakeholders including suppliers and NGOs, and leadership companies in other sectors.

Meanwhile, we continue to drive compliance related to working hours with our suppliers. This can be resolved by hiring additional personal, purchasing equipment, building a dormitory or implementing sustainable demand management.

Some 17% of the supplier sites with this non-compliance are being phased out, however, contingency planning is required before phase-out can occur. Because many of these issues were identified in audits conducted toward the end of 2007, corrective action plans will be implemented in early 2008.

The second most frequent non-compliance was regarding wages and benefits. Corrective action plans are running. As with working hours, this labor issue requires broad public-private cooperation to create sustained improvement.

Regarding occupational health and safety, lack of personal protective gear and life threatening electrical open contacts were found as well as non-preparedness for fires. Most of these improvements are running and will be monitored to ensure continued compliance.

We found that 45% of initial audits require Environmental Management Systems. As previously stated, we will follow their progress until they are certified.

One supplier, for example, engaged in a social project with an occupational school, which involved placing a student in a working environment. The school's legal obligation was to provide only students aged 16 and above, but the school did not meet this requirement and the supplier had not double-checked. In future all students will have to go through the suppliers' standard new employee screening program. This issue was resolved within a month, with the full cooperation of the supplier.

In 2007 we phased out some 30 suppliers due to sustainability reasons. Our overall approach is one of finding solutions through open and honest discussions with the supplier, but if no satisfactory solution can be found, suppliers can expect that this will affect the business relationship.

While some issues took longer to resolve than we had anticipated, we gained speed and resolved 13% of the zero-tolerance issues identified in 2007 during the course of the year. We will work to further reduce throughput time in 2008.

NPR supplier audit results

Our non-product related (or non-sector related) spend includes about 800 key suppliers managed by seven NPR commodity teams.

For each commodity, a risk profile was established and suppliers mapped. A total of 47 risk suppliers was identified and audited in 2007. Key risk commodities were identified in the areas of waste disposal and recycling services, food services, temporary labor, business gifts, printed material and road transport. Ocean transport was also assessed but was not identified as a key risk.

The issues found through these audits differ from Bill of Material suppliers. Temporary labor for example, has been identified as an area of focus. Issues related to

health and safety outnumbered labor issues. Non-conformances are being addressed in a corrective action plan.

Sustainable NPR procurement

As part of our ongoing efforts to minimize our environmental impacts, as well as meet our EcoVision4 targets, our commodity teams have a number of projects underway in the areas of marketing and sales and carbon footprint reduction.

Marketing and sales: Paper

To fulfill our quality and sustainability needs, we work with South Africa-based Sappi, the world's largest producer of coated fine paper. The company is active more than 100 countries, manages its own sustainable forests in South Africa and is committed to initiatives such as the Sustainable Forestry Initiative and the Program for the Endorsement of Forest Certification Systems.

The papers are produced in mills accredited with ISO 9001, 14001 and EMAS certification and Sappi is the first paper company in Europe to hold group chain-of-custody certification for its entire European operations under both the Forest Stewardship Council (FSC) and the Programme for the Endorsement of Forest Certification (PEFC) schemes.

Because paper is usually sold through merchants and printing companies typically purchase paper for their clients, we address the entire supply chain. We have reduced the number of printers we use worldwide to ensure only Sappi's Magno is used for our printed materials.

In addition, we have extended the process of selecting sustainable suppliers to cover inks and coatings to ensure we use sustainable materials for all printing requirements.

Professional and personnel: Leased cars

In 2007 we sharpened our existing green lease car policy to further decrease emissions. In addition to the standards that were already in place on emissions, engines and carbon filters, we include the cost of fuel into the lease price. This will raise user's awareness and provide incentive to lease smaller vehicles.

Travel

For many years, of course, our employees around the world have been making their travel arrangements online. We use both paperless tickets and credit card statements. In 2007 we added a new functionality when employees book their travel – a pop-up window that suggests video-conferencing as an alternative to raise awareness and encourage people to consider this option.

Or car rental policy already stipulated the use of small vehicles. Working with our rental car provider, we added the option of renting a hybrid in 2007.

Facility management and energy

In 2007, 11 of our industrial sites purchased green electricity, generated from renewable energy sources. As a result, CO_2 emissions from industrial sites were 3% lower than they would otherwise have been, reducing our operational carbon footprint by 1%. We are looking to extend this program during the course of 2008.

Forwarding and distribution

Our policy is to use the method of transportation that has the lowest CO_2 impact per kilometer, balancing business needs and environmental impact. This clearly requires mature demand planning. We are also running a program on freight consolidation/deconsolidation to eliminate "empty" kilometers by ensuring maximum loads per kilogram on both outbound and return trips.

We are promoting e-billing and are working with freight companies that use clean engines.

Industrial

In Europe we work with carbon neutral suppliers for wood pallets used at our manufacturing sites. This includes a pallet pool (rental) program and the supplier also plants trees to compensate for the resources used to make the pallets. During 2008 we will work to extend this program into other regions.

We have a program called "leak seek" to prevent inefficient leakage in compressed air systems.

Our office supplies program includes the use of ecologically friendly paper for copiers, note pads, etc.

Stakeholder engagement

Together with the EICC, we have been in contact with several global NGOs that focus on labor conditions. We have listened to their comments on the EICC code.

As mentioned previously, to safeguard the level of standard set by Philips, we have included an appendix elaborating further on employees rights related to freedom of association/collective bargaining in our Supplier Sustainability Declaration.

We also have taken comments asking for solid improvement seriously, and have made an effort to provide a clear view on issues resolution in this report.

During the course of 2007, we were asked to share our expertise on supplier sustainability in various countries where governments have the stated objective of sustainable purchasing. Other companies have also requested that we share information about our supplier sustainability program and universities are now also focusing on this important topic. Our goal is to not only share our approach, but to listen to these stakeholders and learn from them.

We look forward to further constructive dialogue with all relevant stakeholders in the chain.

Recognition

Responsible Supply Chain Management Award

We are proud to have earned the Responsible Supply Chain Management Award in the Netherlands, ahead of 31 other multinational companies, listed on the AEX. According to a survey by the Association of Investors for Sustainable Development (VBDO), Philips achieved the highest score and also made the strongest improvement. The survey also noted that Philips provides the most comprehensive reporting on the sustainable business practices of its suppliers worldwide.

2008 activities in supply sustainability (BOM and NPR)

We will continue to strengthen our Supplier Sustainability Program, further embedding it throughout our supply management organization. Plans for 2008 include:

- Resolving new zero tolerance issues identified in our audits within the specified time. This will be supported by deployment of related scoring in the business balanced scorecard within Supply Management all through the company.
- Ensuring sustainable resolutions. This includes conducting additional surprise audits for selected topics to monitor whether corrective actions have been properly implemented.
- Implementing the full EICC audit checklist of January 1, 2008, adding management systems and ethics.
- Working with all in the chain to ensure sustainable demand management.
- Working with suppliers to improve their energy efficiency and reduce their carbon footprint.
- Continuing to align for next steps in the implementation of the EU REACH Regulation (registration, evaluation and authorization of chemicals).

Materiality matrixes

Page 21 illustrates how we map key material issues for our company. This mapping is based on global trends in the areas of health, business, societal and environmental.

The matrixes shown here include all of the relevant issues from which the materiality matrix on page 21 is derived.

Materiality matrix
Health trends and issues

- These issues are classified as material, and are covered in this report
- Issues in these squares can become material and may be covered in future reporting

- Opportunities
- Risks

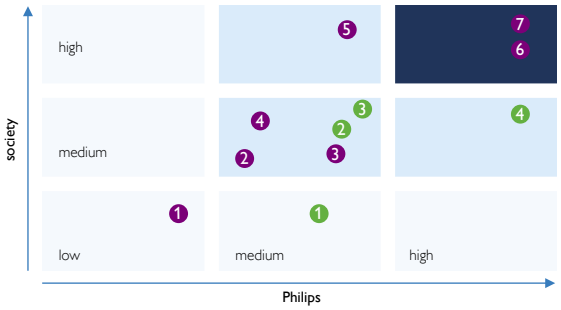
1 Infectious diseases in developing world
2 Chronic diseases in developing world
3 Lack of access to affordable healthcare
4 Rising healthcare costs

1 Treat of epidemics
2 Animal testing
3 Product safety
4 Employee health and safety

Materiality matrix
Business/economic trends and issues

- These issues are classified as material, and are covered in this report
- Issues in these squares can become material and may be covered in future reporting

- Opportunities
- Risks



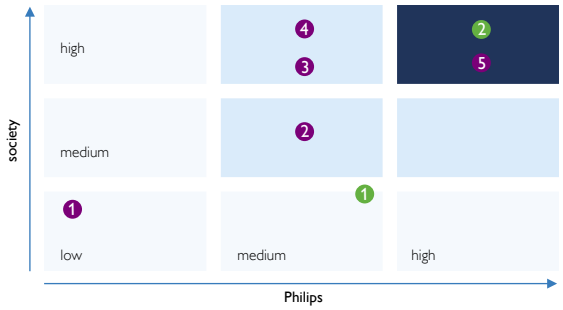
1 New business models
2 Knowledge management
3 Clean Tech
4 New and emerging markets

1 Attractiveness of services
2 Shift from West to East
3 Disintegration of value chains
4 Intellectual property
5 Transparency and accountabillity
6 Business integrity
7 Off-shoring/outsourcing

Materiality matrix
Societal trends and issues

- These issues are classified as material, and are covered in this report
- Issues in these squares can become material and may be covered in future reporting

- Opportunities
- Risks



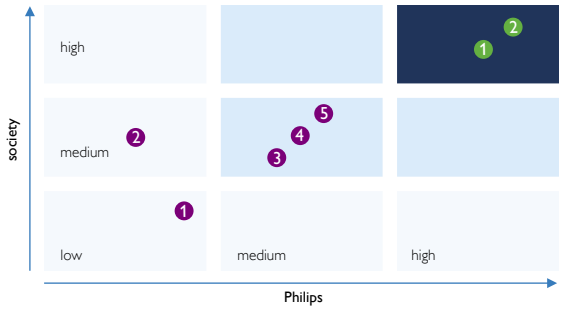
1 Emerging roles of industries and NGOs
2 Aging population in developed world

1 Digital divide
2 Instability / terrorism
3 Privacy
4 Growing population in developing world
5 Rising attention on human rights

Materiality matrix
Environmental trends and issues

- These issues are classified as material, and are covered in this report
- Issues in these squares can become material and may be covered in future reporting

- Opportunities
- Risks



1 Energy management
2 Climate change

1 Waste management
2 Clean air and water
3 Limited natural resources
4 Take-back and recycling
5 Use of chemicals in products

Global Reporting Initiative (GRI): G3 Core Indicators

The *Philips Sustainability Report 2007* addresses the issues that are material for the company with a particular focus on energy efficiency and healthcare. Additionally we report on the three areas of sustainability: economic, environmental and social. This chart provides you with a view of Core Indicators covered in the report. Because our report covers the Philips Group level, Core Indicators on local issues have not been addressed.

			Sustainability Report 2007			
	G3 Numbering		Not applicable	Addressed	Not addressed	Page number
Economic						
Economic performance	EC1	Direct economic value generated and distributed, including revenues, operating costs, employee compensation, donations and other community investments, retained earnings, and payments to capital providers and governments.		●		88-91
	EC2	Financial implications and other risks and opportunities for the organization's activities due to climate change.		●		20-45, 80-84
	EC3	Coverage of the organization's defined benefit plan obligations.		●		90
	EC4	Significant financial assistance received from government.			●	
Market presence	EC6	Policy, practices, and proportion of spending on locally-based suppliers at significant locations of operation.			●	
	EC7	Procedures for local hiring and proportion of senior management hired from the local community at significant locations of operation.		●		76-77
Indirect economic impacts	EC8	Development and impact of infrastructure investments and services provided primarily for public benefit through commercial, in-kind, or pro bono engagement.		●		37, 61

	G3 Numbering		Not applicable	Addressed	Not addressed	Page number
Environment						
Materials	EN1	Materials used by weight or volume.			●	
	EN2	Percentage of materials used that are recycled input materials.			●	
Energy	EN3	Direct energy consumption by primary energy source.		●		24-25, 85
	EN4	Indirect energy consumption by primary source.		●		24-25, 85
Water	EN8	Total water withdrawal by source.		●		85
Biodiversity	EN11	Location and size of land owned, leased, managed in, or adjacent to, protected areas and areas of high biodiversity value outside protected areas.	●			
	EN12	Description of significant impacts of activities, products, and services on biodiversity in protected areas and areas of high biodiversity value outside protected areas.		●		38
Emissions, Effluents, and Waste	EN16	Total direct and indirect greenhouse gas emissions by weight.		●		85
	EN17	Other relevant indirect greenhouse gas emissions by weight.		●		85
	EN19	Emissions of ozone-depleting substances by weight.		●		85-86
	EN20	NOx, SOx, and other significant air emissions by type and weight.			●	
	EN21	Total water discharge by quality and destination.			●	
	EN22	Total weight of waste by type and disposal method.		●		85
	EN23	Total number and volume of significant spills.		●		86
	EN26	Initiatives to mitigate environmental impacts of products and services, and extent of impact mitigation.		●		23, 80-85
	EN27	Percentage of products sold and their packaging materials that are reclaimed by category.	●			
Compliance	EN28	Monetary value of significant fines and total number of nonmonetary sanctions for non-compliance with environmental laws and regulations.	●			
Product responsibility						
Customer Health & Safety	PR1	Life cycle stages in which health and safety impacts of products and services are assessed for improvement, and percentage of significant products and services categories subject to such procedures.		●		23, 56, 81-85
Product and Service labeling	PR3	Type of product and service information required by procedures, and percentage of significant products and services subject to such information requirements.			●	
Marketing Communications	PR6	Programs for adherence to laws, standards, and voluntary codes related to marketing communications, including advertising, promotion, and sponsorship.		●		73-75
	PR9	Monetary value of significant fines for non-compliance with laws and regulations concerning the provision and use of products and services.			●	

	G3 Numbering		Not applicable	Addressed	Not addressed	Page number
Labor practices & decent work						
Employment	LA1	Total workforce by employment type, employment contract, and region.		●		72-73
	LA2	Total number and rate of employee turnover by age group, gender, and region.		●		72-73, 76
Labor / Management Relations	LA4	Percentage of employees covered by collective bargaining agreements.			●	
	LA5	Minimum notice period(s) regarding significant operational changes, including whether it is specified in collective agreements.			●	
Occupational Health & Safety	LA7	Rates of injury, occupational diseases, lost day's, absenteeism and total number of work-related fatalities, by region.		●		78
	LA8	Education, training, counseling, prevention and risk-control programs in place to assist workforce members, their families, or community members regarding serious diseases.			●	
Training and Education	LA10	Average hours of training per year per employee by employee category.			●	
Diversity and Equeal Opportunity	LA13	Ratio of basic salary of men to women by employee category.			●	
	LA14	Composition of governance bodies and breakdown of employees per category according to gender, age group, minority group membership, and other indicators of diversity.			●	
Human rights						
Investment and procurement practices	HR1	Percentage and total number of significant investment agreements that include human rights clauses or that underwent human rights screening.		●		92-101
	HR2	Percentage of significant suppliers and contractors that have undergone screening on human rights and actions taken.		●		92-101
Non-discrimination	HR4	Total number of incidents of discrimination and actions taken.		●		74, 98
Freedom of association and collective bargaining	HR5	Operations identified in which the right to exercise freedom of association or collective bargaining may be at significant risk, and actions taken to support these rights.		●		74, 98
Child labor	HR6	Operations identified as having significant risk for incidents of child labor, and measures taken to contribute to the elimination of child labor.		●		74, 98
Forced and compulsary labor	HR7	Operations identified as having significant risk for incidents of forced or compulsory labor, and measures taken to contribute to the elimination of forced or compulsory labor.		●		74, 98
Society						
Community	SO1	Nature, scope, and effectiveness of any programs and practices that assess and manage the impacts of operations on communities, including entering, operating, and exiting.		●		44-45
Corruption	SO2	Percentage and total number of business units analyzed for risks related to corruption.		●		72-74
	SO3	Percentage of employees trained in organization's anti-corruption policies and procedures.		●		72-74
	SO4	Actions taken in response to incidents of corruption.		●		72-74
Public policy	SO5	Public policy positions and participation in public policy development and lobbying.		●		10-12, 29, 31-34, 49
Compliance	SO8	Monetary value of significant fines and total number of nonmonetary sanctions for non-compliance with laws and regulations.			●	

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Healthcare Informatics
Home Healthcare Solutions
Customer Services

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Lamps
Professional Luminaires
Consumer Luminaires
Lighting Electronics
Automotive and Special Lighting Applications
Solid-State Lighting Components & Modules

Consumer Lifestyle
Connected Displays
Shaving & Beauty
Video & Multimedia Applications
Domestic Appliances
Audio & Media Applications
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