



Philips CEO Gerard Kleisterlee is streamlining this 116-year-old Dutch company.

CEO Interview

From Lightbulbs to Spa-like MRIs

Gerard Kleisterlee, Philips

Twenty-some years ago, when Gerard Kleisterlee was rising fast at \$36 billion Royal Philips Electronics, he had the awkward situation of supervising one of his father's friends. But he didn't need to worry. He received the ultimate compliment: "Your son talks like a regular guy," the friend told Kleisterlee's father.

While that may not seem wildly complimentary, Kleisterlee knows that few skills are more important than communication. The German-born chief executive is an electrical engineer by training who joined Philips in 1974. His natural leadership and strong analytical skills eventually led to his taking the CEO post in 2001.

Once at the controls, Kleisterlee, 60, essentially put the 116-year-old consumer-product titan into one of its own blenders and hit "whirl." Philips sold its volatile semiconductor business for \$10.7 billion in 2006, along with its mobile-phone units. It added seven companies to its already fast-growing medical group, which makes everything from room-size CT scanners to needle-size fetal electrodes. Through divestitures, attrition and some layoffs, the staff of 210,000 was chopped by more than half.

The result: a streamlined company with distinct businesses in consumer products, professional health care and lighting. The company's stock has gone up 60 percent in the past three years as Kleisterlee has refined his mix. But if the once unassuming lightbulb company has come a long way, others think it must go even further. Sanford C. Bernstein analyst Scott Geels says the company should sell some of its investments and consider a splashier, more meaningful acquisition. Philips has lowered its stakes in both Taiwan Semiconductor and France's Ommic, Kleisterlee notes, adding, "It takes time to turn a ship."

Senior writer **Dyan Machan** sat with Kleisterlee in Philips's steel-blue Amsterdam office tower, where he relaxed in an open-collar shirt and reflected on the sweet spots of his business, how change never happens fast enough and why he wants his employees to make more mistakes.

How have "new" Philips products grown out of the old?

We have a light clock that gently and naturally wakes you. Creating it blurred the

traditional boundaries between marketing, consumer appliances and lighting to create a product that fits with our aspirations in health and wellness.

And the old Philips?

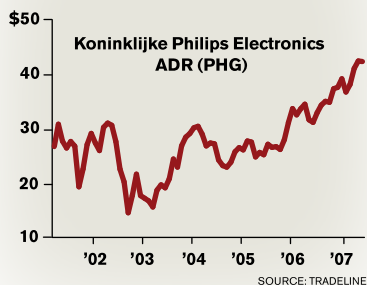
We had a silo culture and would come up with great technology that would miss the market entirely. In the early 1990s, we launched an interactive compact disc platform, but no one considered whether consumers wanted it.

You've brought consumers nearly commercial-free shows, and now you're offering a free directory service for mobile-phone users. Why don't you just send us all a check?

That might defeat our purpose. Our constituencies are all different, but we mainly cater to 35- to 55-year-olds with at least \$70,000 in income who buy flat-screen TVs, have the wisdom to take care of their bodies and care about saving energy. That's not everyone.

NOT JUST BULBS

Kleisterlee has focused Philips on health care, consumer products and lighting.



Are you concerned consumers equate your brand with lightbulbs?

Yes. You could find us somewhere on the box of Norelco shavers, Sonicare toothbrushes and Marantz receivers—but you'd have to look. We're raising the visibility of the Philips brand. One problem is that we've acquired five health care companies in 18 months, and it takes time before all the products are brought together under

our umbrella.

Your health care division has grown to \$9.1 billion today from \$6.5 billion in 2001. Tell me why I can look forward to my next MRI and why health care is such a great business.

Using our lighting technology, we have created a soothing, spa-like experience so

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that MRI patients, especially children, no longer have to be sedated.

Why health care?

Because of the growing demand for medical technology, margins are higher and the business grows at double digits. Nowadays, 55 percent of our medical products are less than two years old.

What's taking you so long to transform?

It's been six years, and you say you're still not done.

We'll never be done. For instance, we couldn't sell our semiconductor business in a down market. You can't sell a problem; you can only give it away. We had to manage it into a good business and wait for the depressed cycle to improve.

You've stated a goal to have companywide operating margins exceeding 7.5 percent.

So why not cut loose your commodity-like electronics business, which has barely 5 percent margins?

You sell the business, you sell the brand and its distribution. Even if it's less profitable, it's still relevant to consumers. Plus it requires zero working capital—meaning we get paid before we pay our suppliers.

That shines a different light on it.

Speaking of which, you use the word "revolutionary" to describe what's coming from LED technology. What's the big deal?

LEDs are so small they give light designers freedom of form that is impossible for incandescents. We are lighting Buckingham Palace for the first time because the light can be directed outward, assuring privacy for the inhabitants. We are also in a shootout for the Empire State Building [Philips won, as it has since acquired its shootout

competitor Color Kinetics]. With LEDs, homes can have different-color tones of light with the touch of a remote. Plus, LEDs save 80 percent electrical energy.

You have a keen interest in the world's moving toward energy-efficient lighting.

Care to make your save-the-planet pitch?

Lighting consumes 20 percent of the global electricity bill; the commercial and public segment composes 80 percent of that. Using the high-intensity discharge outdoor lighting in malls and stadiums can save 50 to 80 percent of energy costs. Consumers can save the same by switching from incandescent lights to energy-saving bulbs.

But consumers must pay six times as much for these bulbs!

But the lifetime is six times as long, and the cost of electricity is lower.

You are known to be blunt speaking.

What are you telling the troops these days that they may not want to hear?

I always tell them the way it is. We had a risk-averse culture and too much bureaucracy. I cut out an entire layer of decision makers. I want them to take more chances.

More risk means more mistakes.

I want them to make more mistakes. Of course, they may make that mistake only once.