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PRESENTATION

Operator

Ladies and gentlemen, welcome to the Signify earnings call. (Operator Instructions)

I would now like to give the floor to Robin Jansen, Head of Investor Relations. Mr. Jansen, please go ahead, sir.

Robin Jansen - *Signify N.V. - Head of IR*

Thank you, Sarah, and good morning, everyone. Welcome to the Signify Earnings Call for the Third Quarter Results 2019. With me are Eric Rondolat, CEO of Signify; and Stéphane Rougeot, CFO.

In a moment, Eric will take you through the third quarter business and operational performance. Stéphane will then tell you more about the financial performance in the third quarter. Eric will end today's presentation with the financial outlook for the year and some concluding remarks. After that, we will be happy to answer your questions.

The press release and the related slide deck were published at 7 a.m. CET this morning. Both documents are now available for download from our Investor Relations website. A full transcript of this conference call will be made available as soon as possible on our Investor Relations website.

With that, I will now hand over to Eric.

Eric Rondolat - *Signify N.V. - Chairman of the Board of Management & CEO*

Thank you, Robin. Good morning and thank you for joining us today. Let's go to Slide 4 with the main elements of our performance for the third quarter. Comparable sales declined by 5%, as we were impacted by a highly -- by the high comparison base in lamps due to the halogen bulb ban in Europe that came into effect in Q3 2018. In addition, we faced a more challenging macro environment, with lower market activity in Europe, U.S., Greater China as well as a major impact of tightening liquidity in India.

Our LED-based sales increased on a comparable basis by 2.6% to 78% of sales, and our installed base of connected light points increased from 50 million in Q2 to 53 million this quarter. We continued to make good progress in reducing our cost base. Excluding the impact of currency movements, our adjusted indirect cost decreased by EUR 22 million, a reduction of 4.7%.

Our adjusted EBITA margin was down 100 basis points to 11% due to the high comparison base in lamps and 30 basis points negative impact from currencies. Our net income slightly decreased to EUR 74 million, mainly due to lower operational profitability and higher restructuring costs. Our free cash flow amounted to EUR 45 million, which included a positive impact of EUR 18 million from IFRS 16. The level of free cash flow reflects the reversal of the phasing of payables and receivables of around EUR 60 million that we talked about when we published our Q2 numbers. When we announced our Q2 results, we also announced the acquisition of Klite, which we have successfully closed on the 1st of October.

Last but not least, sustainability is, as you know, a very important focus area for us. We are, therefore, pleased and proud to have been named industry leader in the Dow Jones Sustainability Index for the third time in a row.

Let's now move to Slide 5, where we can see a snapshot of the financial performance of our growing profit engines. Our growing profit engines grew by 1% on a comparable basis, despite the more challenging macro environment in various regions that I've just talked about. Our growth platforms, connected systems, IoT platform services, horticulture, solar and LiFi continued to show a positive momentum. The adjusted EBITA margin of the growing profit engines increased by 80 basis points to 11%, with each of the 3 business groups improving on the profitability.

Let me now provide you with more details of each of our 3 growing profit engines, starting on Slide 6 with LED. Comparable sales increased by 0.9%. Led lamps delivered a solid performance, while we see price erosion slowing down on a sequential basis. On the other hand, LED electronics continued to be impacted by lower demand from OEM customers in most of the regions. The adjusted EBITA margin continued to improve with an increase of 30 basis points to 12.3%, mainly as a result of ongoing procurement savings.

On the next slide, Slide 7, you can see some of the business highlights of this quarter for LED. In the U.S. and India, we recently introduced our Wi-Fi-based smart home lighting. This provides consumers with very easy to install smart lighting, which operates with the WiZ Connected ecosystem via the WiZ app.

Another highlight is the launch of the new family of plug-and-play constant voltage drivers. So these drivers are very quick and easy to install as they can even be installed by non-electricians.

Let's move now to Slide 8 to talk about Professional. Comparable sales increased by 1.7%, mainly driven by a solid performance in China and the Middle East, which was partly offset by a low level of market activity in India and in Europe, most notably in Germany. Third quarter performance benefited from solid execution of our order backlog and project pipeline, most notably in the Middle East and China. The adjusted EBITA margin improved by 60 basis points to 12.3% as procurement and indirect cost savings more than offset the negative impact of price and mix.

There's a couple of business highlights that I would like to bring to your attention on Slide 9. Let me start with Atea's living lab in Stavanger in Norway, where we combine our connected lighting technology with Cisco's network technology and transform the office into a showcase for the future. Our connected lighting allows employees to personalize the light above their desk, check meeting room occupancy and find free desks and colleagues. It also allows them to tailor room temperature. Guests at the reception of Atea can use our LiFi systems to have a first-hand experience of high speed, reliable and secured wireless connection.

We also installed our Trulifi systems at the press center of German football club HSV in Hamburg. Journalists in the press center of the Volkspark Stadium can file their stories using Trulifi. It solves the issue of wireless signal overload, helping reporters to file stories and photographers to send through their pictures in a reliable, fast and highly secure way.

Let's now turn to Slide 10. Home reported a decrease in comparable sales of 3.1%. While Europe continued to show good momentum, performance in the U.S. was lower due to a strict application of our commercial policies. We made several investments to prepare the launch of innovative offerings in Q4. The adjusted EBITA margin of minus 2.6% represents an improvement of 430 basis points compared with last year and shows a significant reduction of our breakeven point along the year.

For Home, we would also like to share a couple of business highlights with you on Slide 11. In the third quarter, we introduced the Philips Hue Play HDMI Sync box. This great innovation provides an easy way to synchronize all digital content with up to 10 Philips Hue lights. It's compatible with movies, TV shows and games, and it creates a fully immersive viewing experience.

We also introduced the Philips Hue Smart plug. With this smart plug, any table or floor lamp can be turned into a hue-controlled light.

Let me now move to our cash engine Lamps on Slide 12. Comparable sales decreased by 25.5% due to the very high comparison base related to the halogen bulb ban in Europe in Q3 2018. This decline is nevertheless lower than the market decline, resulting in continued market share gains. The adjusted EBITA margin remained solid at 19.4% as a result of ongoing indirect cost reductions.

Next, while we focus on organic growth, we also announced last week that we have reached an agreement with Eaton to acquire Cooper Lighting Solutions for USD 1.4 billion, as you can see on Slide 13. This acquisition will expand our position in the attractive Northern American market and will result in increased innovation power and more competitive offerings. Through the transaction, we will improve our business mix with Professional revenues increasing from 42% to 53% of our total revenues.

The acquisition offers a substantial value creation potential, including cost synergy potential savings of more than USD 60 million per year to be largely achieved in the first 3 years. Mid-teens EPS accretion in year 1 and a transaction ROIC that will exceed our WACC after year 1.

So basically, this is what I wanted to cover with you regarding the business and operational performance. I will now hand over to Stéphane, who will tell you more about the financial performance for the third quarter of 2019.

Stéphane Rougeot - *Signify N.V. - CFO & Member of the Board of Management*

Yes. Thank you, Eric, and good morning, everyone. So let's move now to Page 15 and look at the adjusted EBITA bridge. As you can see here, the adjusted gross margin as a percentage of sales decreased by 120 basis points to 37.9% in the third quarter of 2019. And this is only due to the lower sales volume in lamps, given the very high comparison base.

When you look at the gross margin of the growing profit engines, actually, it was stable in the third quarter compared to last year. The impact on the price on the overall gross margin was lower than in the third quarter of last year. And as usual, we've been able to largely offset that negative price impact by the ongoing savings in our cost of goods sold.

We've continued to take actions on our cost and the indirect cost base decreased by EUR 22 million compared with third quarter of 2018, taking out the impact of ForEx. Finally, when we look at the FX impact and the prevailing spot rates at the end of September, we expect the currency impact on the adjusted EBITA margin for the fourth quarter of 2019 to be around 20 basis point -- positive 20 basis points. And therefore, for the whole year to be negative 30 basis points.

Turning to Page 16. You can see the evolution of our indirect cost base. The initiatives that we have taken, or continuing to take, have resulted into EUR 22 million of currency comparable indirect cost savings in the third quarter, and this is close to 5% reduction year-on-year. We had a negative impact of ForEx on our cost base by EUR 6 million. So we are quite satisfied with the evolution of the indirect cost base. We've done EUR 224 million of cost savings on a currency comparable basis in 2019 -- sorry, in 2018. And when you look at year-to-date, we are already at EUR 98 million. We continue to execute many initiatives in order to further decrease our indirect cost base, and we expect to deliver, again, a solid improvement in the indirect cost as a percentage of sales for the full year 2019.

Let's now take a look at the working capital of the third quarter on Page 17. So when you compare with the same period of last year, you can see that the working capital decreased by EUR 71 million and reached EUR 588 million at the end of September. As a percentage of sales, this is a decrease of 70 basis points and our working cap represents 9.4% of sales, and that was mainly the result of lower receivables and also higher payables. The inventories on the right side increased by 130 basis points to 16.5%. As you know, our inventories are generally higher at the end of the third quarter to prepare for a seasonally strong fourth quarter. So the year-on-year increase in our inventory can be explained by higher inventories in home and also in Europe, which are partly offset by improved inventory levels in the Americas.

Finally, let's take a look at our cash and debt position in the following slide. Our net debt decreased by EUR 8 million compared to the level at the end of June. So of course, we generated a profit in the quarter and also the change in working capital that I have just mentioned. And you can see also the other items in the bridge that impacted our cash and therefore our debt position.

Our net CapEx was EUR 8 million in the quarter, and the net change in provision was EUR 23 million. Next to that, we paid for tax and interest an amount of EUR 28 million. The other bucket on the right of EUR 38 million is higher than what it used to be in previous years because it now includes the new lease liabilities following the application of IFRS 16, and it's also here the FX impact on cash, cash equivalent and debt. All in all, our net debt position amounted to EUR 857 million at the end of the third quarter, and that includes the lease liability as per IFRS 16 that is applied since January 2019.

Let me now hand back to Eric for the final part of the presentation.

Eric Rondolat - *Signify N.V. - Chairman of the Board of Management & CEO*

Thank you, Stéphane. Let's go to the outlook on Slide '20. Due to the challenging macro environments that we are currently facing, we have revised our outlook for 2019. We remain confident that we will be able to improve the adjusted EBITA margin for 2019. However, somewhat less than the ambitious level we had set previously. We now expect the adjusted EBITA to be in the range of 10.3% to 10.6% for 2019.

As it comes to sales, we expect the CSG of the growing profit engines to be flat. The CSG of the business group Lamps is expected to decline towards the higher end of the previously indicated range of minus 21% to minus 24%. In other words, closer to minus 21%. And lastly, we confirm that our free cash flow, excluding the positive impact of IFRS 16, is expected to be above 5% of sales.

With that, I would like now to open the call for questions, which Stéphane and myself are happy to answer.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) And our first question comes from the line of Lucie Carrier from Morgan Stanley.

Lucie Anne Lise Carrier - *Morgan Stanley, Research Division - Executive Director*

I'll go one at a time. The first one, Eric, Stéphane, maybe can I ask a bit of a difficult question. But the new guidance you are giving on adjusted EBITA is substantially below the one you had before. And even the low end of the previous guidance is not even embedded in the new one. Can I ask what has changed really over the last few months that kind of triggered this outlook? And I guess, what I'm trying to understand is, what has been really the variation versus your expectation? In which division have you seen really the biggest shortfall? So that's my first question.

Eric Rondolat - *Signify N.V. - Chairman of the Board of Management & CEO*

Yes, Lucie. So effectively, we've seen a worsening of the end market situation in Q3. And with all the discussion we have on a regular basis with our markets, and specifically, when we did the forecast for the upcoming quarter in Q4, we don't think that there will be a sufficient improvement of that situation. So we maintain the original guidance.

In July, we thought that we were entering H2 with the most -- with a more favorable base of comparison on many businesses. We have stated at that time, Q3 will be more favorable for LED and Q4 will be more favorable for Professional, which is mathematically the case, but we've seen further degradation of the end markets. That's the case in Europe. And in Europe, most notably in Germany, which is a very important market for us. And something that was not at all expected when we did our Q2 announcement is the situation in India, where we have been facing a situation of basically tightening of liquidity. Now we are not the only company that is facing that situation, you can hear that from many other people. And that situation is really impacting us in Q3, and we believe it is going to impact us until probably the mid of next year. That's what the economic analysts are saying at this point in time.

So if you take a bit of distance, India, for us, it's a country in the top 5. I think in our annual report, you will find that we invoiced EUR 416 million last year. So it's an important market for us, where we are leading powerhouse, and we didn't at all expected the situation that we are facing and that we believe will continue over the upcoming quarters.

So that situation is not allowing us to grow at the expected levels. When you don't grow at the expected levels, you can always try and adapt on the rest of the P&L, which is what we're trying to do. But we don't think that we're going to be capable to do it, to be in line at least with the 11%, which was the lower level of the guidance that we gave at the time of the IPO and that we confirmed systematically over the past 4 years. Now the good news is still that within challenging market conditions that have been worsening all along the year, we still believe and confirm that we're going to be able to further improve on our operating margin by 30 to 60 basis points for the full year. So this is basically the story, Lucie.

Lucie Anne Lise Carrier - *Morgan Stanley, Research Division - Executive Director*

My second question was on the Home business. Can you maybe explain how we should think about this business? Because to me, the growth seems to be still a little bit disappointing, especially considering you had a negative comp last year. And of course, it's still not really profitable. So is that, that you're seeing more competition? Or do you see more pricing pressure? And in your comments actually around the division, you've mentioned that you had done in the U.S. a strict application of your commercial policies. So what is precisely going on here, please?

Eric Rondolat - *Signify N.V. - Chairman of the Board of Management & CEO*

I would agree with you saying that the growth is disappointing. The P&L situation is satisfactory. So let me explain. Yes, we were expecting more growth. And in the U.S., we had to have a stricter application and a very strict application of our commercial policy. We were asked to abide by some conditions that we didn't accept from a commercial standpoint. So let me give you a hint. Price matching, guarantee of 100% return for the full first year of introduction of new offers. In some cases, even a margin guarantee for the retailers. So these are things that we do not do. And when we refused these conditions, we were not listed as expected in some of our retailers. Now I see this as a short-term issue. We need also to mark very clearly the boundaries of how we want to operate. And when I'm talking about that, it is more specifically in Northern America because that business has continued to be very strong in Europe.

When you look at the P&L, and this is what is also interesting, if you look at our P&L in the past 3 quarters, we're basically achieving a similar top line revenue. But our bottom line has systematically improved, meaning that we have lowered the breakeven points all along the year. And I think the situation of the P&L in Q3, even if we are still negative from a bottom line perspective, is very well oriented. You know that Q4 is the big quarter for the business. We have released a lot of very exciting innovation, some have commented previously. So we are very excited about the potential that we have in Q4 for that business.

Operator

Our next question comes from the line of Daniela Costa from Goldman Sachs.

Daniela C. R. de Carvalho e Costa - *Goldman Sachs Group Inc., Research Division - MD & Head of the European Capital Goods Equity Research Team*

So the first question I want to ask sort of ties back with the prior comments around margin. You had the medium-term ambition, which then was '19 of 11% to 13%. '19, obviously, you've just commented on what you are seeing. But would you say that sort of medium-term 11% to 13% is still sort of a level that you're -- where your ambition lies? Or has anything sort of structurally changed in the industry or in your own understanding of the margins that you can do medium term?

Eric Rondolat - *Signify N.V. - Chairman of the Board of Management & CEO*

Daniela, nothing has structurally changed. I think we are facing challenging market conditions at this point in time. We will indicate further where we see the company going. But we don't see the company stopping where it is now. From an operating margin standpoint, I think we can structurally do more in the future.

Daniela C. R. de Carvalho e Costa - *Goldman Sachs Group Inc., Research Division - MD & Head of the European Capital Goods Equity Research Team*

So the 11% to 13% sort of remains your medium-term ambitions, is that the way to read what you just said?

Eric Rondolat - *Signify N.V. - Chairman of the Board of Management & CEO*

No, I'm not saying that. I'm saying that in due time, we will set a new ambition for the future. And we haven't decided yet what it's going to be. That's why I cannot answer positively to you. But directionally, it will be pretty much in line with what we had said previously.

Daniela C. R. de Carvalho e Costa - *Goldman Sachs Group Inc., Research Division - MD & Head of the European Capital Goods Equity Research Team*

Got it. And then just one more quick follow-up on -- because I think when you did the Cooper Lighting call, I'm not -- I don't think we've discussed sort of any charges or one-offs that you would have to incur towards that, sort of, in the preparation for that. But when we think about forecasting 2020 free cash flow and even Q4 free cash flow, is there anything that we should be aware of in terms of charges that you will incur leading up to the deal?

Stéphane Rougeot - *Signify N.V. - CFO & Member of the Board of Management*

Yes, Daniela, this is Stéphane. So yes, when it comes to the overall cost related to the acquisition and also the integration and the synergies, that's something which we are working on. Of course, we have some high-level estimates. But as we are getting and working towards closing, we'll get a better view. And at that point of time, we'll share that.

With respect to short-term impact in Q4, for example, on free cash flow, because we're still going to be between signing and closing, there will be some costs, but they will be limited and much more transaction-related cost than integration-related cost or synergy-related cost by definition because we won't be able to do that.

Leading into 2020, of course, it will be more the case, but then we will communicate at that point of time.

Operator

Our next question comes from the line of Leo Carrington from Crédit Suisse.

Leo Carrington - *Crédit Suisse AG, Research Division - Research Analyst*

On the topic of recent acquisitions, with Klite's deal now closed, can you disclose any additional financial details or observations from that business itself? And also, how much do you expect to pay for it in terms of total consideration?

Eric Rondolat - *Signify N.V. - Chairman of the Board of Management & CEO*

Yes. So on Klite, we gave some indication regarding the financials of that business, meaning revenues, level of profitability. So that's something which was communicated in July when we announced the signing. We haven't given the details of the amount paid. And what we said in July that this is a private transaction with private owners. And in the agreement that we have with them, we cannot disclose the exact price. So you will see in Q4 in our free cash flow because we closed in October, an amount related to that. But we won't be able to disclose a specific price. It's going to be more, yes, impacting in the fourth quarter.

For the rest, we'll provide you maybe on the cycle, the details on the financials of the entity itself. But that's something which we gave in July.

Leo Carrington - *Crédit Suisse AG, Research Division - Research Analyst*

Yes. Understood. And a quick follow-up on Lucie's question. In Home, what factors drove the better performance in Europe versus the U.S.? Is it just this dynamic of you enforcing your commercial terms in the U.S. versus perhaps those being easier to hold in Europe? Or is there something else?

Eric Rondolat - *Signify N.V. - Chairman of the Board of Management & CEO*

It probably has to do with the market structure. I think in Europe, we have many different go-to-market and smaller markets. So basically, you are putting less eggs in the same basket, if I can use that expression, which is a bit different in the U.S. where you have major retailers in front of you. So when things are working fine, well, you get a boost in terms of top line. When you have some adjustments, you may have the counter effect of that very powerful access to the market. So we've been also in Northern America diversifying our access to market, but we -- but it is still fairly concentrated.

Operator

Our next question comes from the line of Martin Wilkie from Citi.

Martin Wilkie - *Citigroup Inc, Research Division - Director*

It's Martin from Citi. So the first question is just around the cost savings. And just to clarify, you commented that the change in margin guidance was really an end market-driven piece. And obviously, on indirect costs, you're now below 29% of sales for the quarter. But I think on a trailing 12-month basis, a little bit above it. And just to clarify, do you still think you can get that number below 29% for the year and therefore, the cost savings are on track? That's my first question.

Stéphane Rougeot - *Signify N.V. - CFO & Member of the Board of Management*

Martin, I don't think we gave specific indications of where we're going to be in terms of cost as a percentage of sales for the year. So I won't be able to give you more details there. I guess, your question is a bit more general on whether we see the potential to continue to reduce our cost and whether we believe we can reach a percentage of sales that is below 29%. And here, the answer is yes. We are continuing to take a number of actions. Of course, 2018 was a very big year in terms of the amount of cost that we've been able to take out. As you look at the following year, first, you have a lower base by definition because you've already taken out quite a lot.

Number two, you have, at the beginning, the impact of the carryover effect of what you've done during the year 2018. And then you start to see the impact of what has happened beginning of 2019 and in the course of 2019, which is now what we see. There is much more limited and there will be much more limited impacts of what we did in 2018 in Q3 and, of course, in Q4 as well. But what we -- what you see now is all the actions that we have taken and that we continue to take. So yes, the potential stays pretty substantial, and we'll continue to do it in Q4 and in 2020, and we have a number of actions so that we end up at a level that will be lower than 29%, but I'm not going to comment whether it's full year 2019 or slightly thereafter.

Martin Wilkie - *Citigroup Inc, Research Division - Director*

Okay. And then just a separate question on LED. I mean, obviously, you saw positive comparable sales growth this quarter, having been negative for the last couple of quarters. Is that just the base of comparison effect? I mean, we can try to estimate what is sequentially. But just trying to understand, sequentially, did LED improve? Or is that better comparable sales growth, just simply a sort of base of comparison effect? And if you could sort of split that between both the lamps and the electronics part of it.

Eric Rondolat - *Signify N.V. - Chairman of the Board of Management & CEO*

Yes. Martin, sure. Yes, the comparison base helps to understand the performance for Q3, as we had originally said. When you look at the 2 businesses, we have a good traction on LED lamps. And we have lower performance on LED electronics, which is also going in sync with the fact that we see the luminaires business slowing down. So we sell LED electronics to other luminaire manufacturers, we call them the OEMs, and we see less business coming from these OEMs because they are themselves selling less. So if you look at the 2 businesses that are making the LED business group today, it's a good traction on LED lamps and is a slowdown in LED electronics.

Operator

Our next question comes from the line of Marc Hesselink from ING.

Marc Hesselink - *ING Groep N.V., Research Division - Research Analyst*

I would like to look a little bit at the lamps division. So clearly, I think as expected, the decline was a bit higher in this quarter. But for the year, you're still running at 21%. So for the quarter to come and also maybe looking at -- into next year, the impacts of the halogen ban will those completely fade away in the coming quarters? Or is that something that goes on for still a few quarters?

Eric Rondolat - *Signify N.V. - Chairman of the Board of Management & CEO*

No, the impact of the halogen ban impacted us last year in Q3 mainly, and partially in Q4. So we're going to have to face this base of comparison. Well, we've faced it in Q3, and you've seen the result with minus 25.5% of CSG, which is much lower than what we experienced previously, but we knew that. There is going to be somewhat remaining effect in Q4, but it's going to be much less than in Q3. And after that, it's going back to a normal situation.

The only thing that we don't know yet because no date has been confirmed is if and when a halogen ban would happen in Northern America. It has happened already in Europe. Normally, North America follows. But we have no information of when that could be. But if ever it happens, once again, halogen is not a technology where we are the most involved and we would be totally capable to face another ban of halogen, whenever it happens, and in the same shape and form than what we've been able to do for the Europe case.

Marc Hesselink - *ING Groep N.V., Research Division - Research Analyst*

Okay. Clear. And maybe then to be 100% sure from my side, if you say that the expected decline is basically at the higher end of the range, minus 24% to minus 21%, is then the higher end of that minus 24% level or...

Eric Rondolat - *Signify N.V. - Chairman of the Board of Management & CEO*

No, it's minus 21% because arithmetically, minus 21% is higher than minus 24%. Here, it's been a big debate internally on how we would phrase that. So -- but that's why in my introductory speech, I highlighted minus 21%.

Marc Hesselink - *ING Groep N.V., Research Division - Research Analyst*

Okay, okay. That's all clear. And then the other question is on India. So now the second quarter that was impacting you, how do you see that recovering going forward because I think structurally, it's still probably a very promising market. But how should we face that?

Eric Rondolat - *Signify N.V. - Chairman of the Board of Management & CEO*

Look, in the midterm and long term, there's absolutely no question. This is a very, very promising market and a market where we are extremely well positioned. Once again, I don't see, at this point in time, any recovery before mid next year, mid-2020, at least this is what the analysts are saying.

Maybe we're speaking from a conservative position today because we thought that India after Q2 would recover. It has not happened. And this situation at this point in time, which is about basically tightening of liquidity, is a complex situation because it's hampering the economical actors on that market. And time to recover is always slow in these cases. So we don't see an improvement in Q4, and we believe that it will not dramatically improve before mid-2020.

Operator

Our next question comes from the line of Wim Gille from ABN AMRO.

Wim Gille - *ABN AMRO Bank N.V., Research Division - Head of Research & Equity Research Analyst*

I would like to go back to the Home division. You basically alluded to the fact that you did not accept the commercial margins or the commercial terms of the big U.S. retailers or some of them. And as a consequence, you were not lined up in the third quarter for basically their sales. Yet you are relatively optimistic, I would say, for your, let's say, capabilities for the fourth quarter going into the holiday selling season. You also have inventories being built up in preparation for that. So how should we look at those discussions around the commercial terms? Have the retailers come around and now you're back on the shelves? Or how should I look into that? That would be my first question. And the second one is on Klite. You highlighted you see cash out in the fourth quarter. Is this going to be your only cash out? Or will there also be an earn-out at a later stage?

Eric Rondolat - *Signify N.V. - Chairman of the Board of Management & CEO*

I will take the first question and I will let Stéphane take the second one. I think that's a very, very good and important question that you asked about that dynamic. So basically, what happened in Q3 happened in Q3. But we continued negotiating or we also have different access to the market. So if we cannot go through one, we can't go -- we can go through another one. But when it happens during the quarter, it's more difficult to recover and to reposition the offer on other channels.

Now we've worked on Q4 in order to improve further our go to market. And I think we have achieved that. While at the same time, what makes me confident for Q4 is the amount of innovation that we are bringing to the market. And I'm going to talk about the Philips Hue offer and picture what we're bringing to the market in Q4.

Bringing to the market in Q4, improved ranges with the Bluetooth capability on ranges like Hue Go, which was a star range in the family. We're bringing filament lamps that are going to be connectable under the Hue system. We're bringing smart plugs. We're bringing smart switches. We're also bringing a totally revolutionary HDMI smart box, where basically you connect all your content, video streaming, gaming to that box, then back to the TV. And then that box synchronizes your digital viewing content with the lights you have in your house. So at the end of the day, we're bringing a lot of very exciting innovation to the market. And those innovations have a direct impact on growing the market and allowing us to grow.

At the same time, it is the biggest quarter in the year. We are ready from an inventory standpoint. So we expect to have a very, very fruitful and very engaging Q4 season. So this is why we are comfortable.

And on the go to market, what we could not do in Q4, we'll find different ways to go -- in Q3, sorry, we'll find different ways to make it happen in Q4.

Wim Gille - *ABN AMRO Bank N.V., Research Division - Head of Research & Equity Research Analyst*

Yes. To summarize, on the one hand, you have tried to diversify, basically, the number of channels that you are able to sell-in. Yet, on the other hand, given the commercial lineup that you have with all the products that you're bringing to the market, you're bringing sufficient leverage to basically get back on the shelves with that particular retailer where you were temporarily kicked off. Is that the way to summarize it?

Eric Rondolat - *Signify N.V. - Chairman of the Board of Management & CEO*

Or others.

Stéphane Rougeot - *Signify N.V. - CFO & Member of the Board of Management*

So Wim, on the Klite question, so there is no earn-out and almost all the payment is done upfront. There is a little bit that is kept in escrow that will be cashed out 1 year from now, but it's a small part.

Wim Gille - *ABN AMRO Bank N.V., Research Division - Head of Research & Equity Research Analyst*

Very helpful. And then a final question from my end, also related to the Home question. We see the momentum in the United States being relatively negative with comparable sales growth minus 10% for the third quarter. It was minus 8% and minus 2% in Q2 and Q1, respectively. So what is driving this negative momentum? Is it fully attributable to the issues that you -- the temporary issues that you have in the Home division? Or is it also that you see, let's say, a weakening momentum in the United States and the other divisions?

Eric Rondolat - *Signify N.V. - Chairman of the Board of Management & CEO*

No, it is attributable to 3 business groups or business units. It's lamps, the conventional lamps, which have declined substantially in Q3 in Northern America. It's LED electronics, I've commented it previously. So we've seen our OEMs buying less. And it's Home that we have just commented on.

Operator

Our next question comes from the line of Joseph Zhou from Redburn.

Joseph Zhou - *Redburn (Europe) Limited, Research Division - Research Analyst*

Eric and Stéphane, I have one for Home division and the other one for Professional. And first, on Home. And you mentioned about this to me, that's the retailer destocking issue. And the large U.S. retailers demands on the change to your commercial policies. And are they mainly focused on your new products or existing products? And have you seen this happened before? And also, what do you see in, is it probably the sellout of those retailers compared to -- relative to the destocking issue? And lastly, if you can -- if I can try. And how much of your revenue is attributed to these large U.S. retailers in the U.S.? And I will give my second question after this.

Eric Rondolat - *Signify N.V. - Chairman of the Board of Management & CEO*

Yes, Joseph, we don't indicate specifically the revenue, which is going through these retailers in the U.S. Nevertheless, the demands are focused on the new, but also on the normal line of business. On the new, specifically, we had a demand of 100% return for full year for all the new offers. So we have a specific demand that only touches the new offers. Otherwise, the rest was pretty much all the business that we do with them. When we look at the selling out, the selling out has lowered compared to what it was in the previous years when it comes to smart home lighting, in general. And this is linked to the fact that there's a lot of positive traction on smart home at large. When we started, lighting was one of the first element that people were actually buying in the smart home. Now you have many opportunities to buy a lot of different things. And when you look at the selling out of the smart home lighting, it is below the average of the selling out of smart home at those retailers. And so we're experiencing the same thing when it comes to the selling out.

Joseph Zhou - *Redburn (Europe) Limited, Research Division - Research Analyst*

Okay. And on Professional and -- can you give us some color on your system and services sales in the quarter and also year-to-date? And also, if we look at the market as a whole? And can you give us some color on the penetration of systems and services by region, U.S. versus Europe versus the rest of the world?

Eric Rondolat - *Signify N.V. - Chairman of the Board of Management & CEO*

So when it comes to systems and services, we see a penetration which is pretty strong in all the regions. The promises of smart systems is energy efficiency which is higher than we -- when we only do the technological change of moving from conventional to LED, but also other collateral benefits. So we see a lot of traction worldwide. We don't give any specific elements on a quarterly basis, we will do that at the end of the year as we do normally. But we are pretty much happy on how our offers are being developed. That it's not only systems, but it is also our IoT platform, Interact, where we are gathering data and trying to monetize this data. So this is a part of the business, which is moving on with more and more customers being, I would say, the right level of education to understand the benefits beyond quality of light and beyond energy efficiency.

Where we see also a very, very good traction is on our new growth platform, namely horticulture and animal lighting. It's 3D printing. It's also solar or LiFi, where we start to have more and more interesting applications that can be derived from that technology. I was talking about this Hamburg Stadium, which is a very interesting one because when you are in a stadium, everything is congested, the Wi-Fi -- because there are too many people. So the Wi-Fi is congested. Even if you try your 4G connection, it's going to be very difficult to send important files and heavy files.

And with LiFi, since we have a reliable, stable, a very fast network, another reporter that is capable to make it happen during the matches. So all these things are new applications that we discover while walking. And well, I think we've made the right investments for the future. These businesses are some of them medium-sized, some of them small, but with a very strong positive momentum.

Joseph Zhou - *Redburn (Europe) Limited, Research Division - Research Analyst*

Yes. Sorry, and just on the installed base penetration of systems and services. Can you give us maybe some kind of a color as to whether U.S. is higher versus Europe or the other way around? And is the difference material?

Eric Rondolat - *Signify N.V. - Chairman of the Board of Management & CEO*

What we see is that, in general, where we have a high market share, our penetration is strong. But from a trend perspective, I would tell you that I see all the markets trending well. We are very successful in some of the big markets in Europe. We're very successful in India. We start now to have a lot of success in China. We see also Middle East after the difficult period that we experienced because of the market slowdown. Now we have a lot of traction on connected street lights. So it's pretty much happening all over the world.

Operator

Our next question comes from the line of Tanuj Mukhija from the Bank of America.

Tanuj Mukhija - *BofA Merrill Lynch, Research Division - Associate*

I have a question on Signify's India operations. So my channel checks with Indian LED manufacturers and retailers suggests that Philips has cut LED prices by 15% in India to push volumes. So can you please provide some color on Signify's pricing and sales strategy for India operations?

Eric Rondolat - *Signify N.V. - Chairman of the Board of Management & CEO*

Well, I happen to have visited India, not so long ago, and we are extremely well connected to the team there. If you go on the market and you look at the prices, I don't think that you will see us as the lower priced on that market. I think we still have a brand premium because of the quality that we deliver because of the width of wallet. Our strategy, the strategy that we have everywhere, innovate in order to be able to grow the market size and bring a higher level of involvement to our consumers.

In India, we are also deploying the Hue offer. And we are also recently launching our Wi-Fi WiZ offers. So as you can see, our strategy in India is pretty much in line with what we do everywhere, which is innovate to create more value.

Tanuj Mukhija - *BofA Merrill Lynch, Research Division - Associate*

Interesting. If I can ask just one follow-up question. What's your opinion on LED prices in the Indian industry overall? Do you think we are at the bottom of pricing erosion? Or is there still some scope of price correction of LEDs in India?

Eric Rondolat - *Signify N.V. - Chairman of the Board of Management & CEO*

That's a very important question. I think you can move it up to a larger territory than only India. I think what is important, it's not only the price of the product, it's whether the manufacturers of these products are at this point in time making money. And if you ask me, I see a lot of actors on the LED lamps because we talked about the LED lamps business. Many actors from Asia. I think there are new actors also coming from India. At the end of the day, you run a business only if it's profitable. There are many actors, many of them are not profitable. We think that the market will have to shake out in the future.

From a technology perspective, we are entering the phase where there's much less cost that we can extract from technology. Now there are always other possibilities and alternative possibilities that, on our side, we will never go to. I can give you examples. We -- people could use recycled materials. So recycled metals, recycled plastics, something that we would never do, because we know that at one stage or another, they will crack. People can also decide to overdrive the LEDs, which we do not do because we believe that it hampers the lifetime of the product, but also the quality of light. So there are many things that can be done to further try and decrease the price of LEDs, but these things are going at the opposite direction of quality. So these are things that we don't do because we don't believe that it serves the market in any way. And I don't think that it gets a customer acceptance in the longer run. We see customers coming back to us telling us that they bought LEDs that we are lasting only for 8 to 9 months, then the color is changing, and they ask us why? And there are a lot of explanations for that. So could that be actors tempted to go for low-quality because at the end of the day, building a lamp which is made of electronics is not that complicated. That's possible. There may be many of them, not many are making money, so they will go at one stage. And I don't think it's a longer-term trend since the quality is not there.

Operator

As we are now approaching the end of the call, we will now take our last question from the line of Akash Gupta from JP Morgan.

Akash Gupta - *JP Morgan Chase & Co, Research Division - Research Analyst*

Eric and Stéphane, I had only one question regarding pricing in the bridge. So at EUR 69 million negative, it was higher than the level we had seen in the first half of the year. So maybe if you can talk about, is there something we should read into it? Or is this just pure mechanical driven by segment mix? And also, if you can update us on where do you stand in your negotiation with respect to bill of materials and some of the component cost?

Stéphane Rougeot - *Signify N.V. - CFO & Member of the Board of Management*

Yes, sure. So yes, EUR 69 million, when you look at the absolute value, you're right. When you compare to Q1 and Q2, we are closer to EUR 57 million, EUR 59 million. And when you go back in time, of course, the amounts were substantially higher. When you apply that to the overall value of revenues in percentage, you actually see overall an improvement. So Q3 this year, the $69 million equivalents to minus 3.8% price reduction. If you look at last year, it was minus 4%. If you look year-to-date for the first 3 quarters, the price reduction is minus 3.6%. Last year, it was minus 4.7%.

So what we've said now for about 6 to 7 quarters is continuing, which is a slowdown of the price reduction. Now then from one quarter to the other, it can be slightly different. But the trend is still there and we still see a slowdown, especially in LED and in LED lamps, in particular, but also across a number of other businesses, a slowdown of the price reduction, so -- and this is what the numbers reflect. Okay, absolute value can be a bit higher because we have higher sales, but the percentages are generally better. So that's how we see it.

Operator

And I would like to return the conference to the speakers.

Robin Jansen - *Signify N.V. - Head of IR*

Okay. Thank you, Sarah. Ladies and gentlemen, thank you very much for attending today's earnings call and for taking part in discussion about our results. If you have any additional questions, please do not hesitate to contact the IR team. And again, thank you very much, and enjoy the rest of the day.

Operator

This now concludes our conference. Thank you all for attending. You may now disconnect.