

## **Sustainability**

For the adidas Group, being a global leader in the sporting goods industry means improving working conditions in our suppliers' factories and reducing our environmental impact as a business. It also means we have to rise to the challenge of managing, supporting and developing over 27,000 employees who work at more than 150 locations in more than 50 countries as well as responding to the needs of the communities where we operate.

Our latest corporate responsibility publication is now available. It describes the steps we took in 2006 to create a unified approach to managing and measuring the adidas Group's social and environmental impacts. Take a look around and let us know what you think of our reporting.

Read an overview of our social and environmental programme.

## OVERVIEW

This is an overview of our social and environmental strategy and programme. For us everything begins with our 'Workplace Standards'. We also describe some of the challenges we face in being a responsible business, and how we are responding to those challenges.

Publishing our progress in meeting our annual targets gives stakeholders a sense of what we have achieved and where we need to do more. Our commitment to being accountable means we also list our targets for the current year. The glossary explains some of the terms we use.

## Our Standards

The adidas Group and its brands have business relationships with manufacturers in many countries around the world. Outsourcing our production in no way absolves us of moral responsibility for the way our products are manufactured and the conditions they are produced under. Recognising this responsibility led us to create a set of guidelines for our suppliers that set minimum social, environmental and health and safety standards we expect them to achieve. We call these our 'Workplace Standards'.

Based on International Labour Organization conventions, the 'Workplace Standards' describe clear rules of conduct for issues such as the environment, safety in the workplace, child labour, and hours of work. By monitoring compliance with the Standards, we can identify potential problems in contract factories and help our suppliers implement positive changes. If they repeatedly fail to do so, we will terminate our contract with them. This however is always the last option we take from a range of other remedies. In short, the 'Workplace Standards' are a tool we use to select and retain only those suppliers whose workplace standards are consistent with our values.

For our 'Workplace Standards', go to the end of this section.

## Challenges and responses

### Global brands – Global visibility

Sport is a universal language and the adidas Group is a global business: we have offices in more than 50

countries and more than 40 nationalities represented among our staff at the Group's Headquarters. We source products from more than 60 countries. In short, our brands are visible all over the world. Current developments that further increase our visibility are:

- The acquisition of Reebok has increased our presence and influence in the international sporting goods business.
- The 2008 Beijing Olympics. These first Olympics in China will draw more attention to the adidas Group with millions of people watching the games. And adidas will be there as official partner and kit provider to many leading athletics nations. From a social compliance perspective, managing this increased visibility is a challenge, as we know from issues raised at previous large-scale events such as the FIFA World Cup™.
- As ever, the way we manage our supply chain is under scrutiny. The end of the Multi-Fibre Arrangement, the consolidation of the supply chain, and the social impact of our sourcing strategy have drawn increased attention from various stakeholders.

Being a highly visible brand that operates in a dynamic competitive environment and sources from a multi-layered supply chain poses specific challenges. We now present those challenges and our responses. In the progress against targets section we provide a more specific summary about our successes and failures in 2006.

### Challenge: Integrating Reebok into the adidas Group

With the addition of Reebok, our supply chain became even more complex. While adidas brand

products are in large part sourced centrally, Reebok products are mostly sourced by individual business units, and often through multiple agents and licensees.

The principal challenge for 2006 was to review every standard, guideline and procedure from both brands, and from those to create a combined social and environmental programme that takes into account a larger business footprint and a more complex supply chain.

**Response: Approach to integration**

We established working groups drawn from senior managers and field staff to critically evaluate all our standards, guidelines and procedures. Our integration work is not complete but we have reached three key milestones. First, we created a new Group-wide set of 'Workplace Standards' that replace the 'adidas Standards of Engagement' and the 'Reebok Human Rights Production Standards'. Next, we established new internal and external procedures covering initial factory assessments and ongoing monitoring of non-compliances and their root causes. And finally, all our assessments are now recorded in our central database – the Fair Factories Clearinghouse. This allows different corporate functions in the adidas Group to communicate more efficiently and to work more collaboratively.

**Challenge: Building credibility and trust**

Some stakeholders have concerns about the credibility of an internal supply chain monitoring programme. The major point of criticism is the independence and impartiality of such programmes. Adverse impacts on working conditions, such as peaks in working hours, may be caused through our own sourcing patterns. The fact that more products are sourced from countries where freedom of association is legally restricted raises further concerns for some stakeholders.

Therefore they argue that we can make only limited progress in improving working conditions. In turn this leads to stakeholders' requests to become transparent in our compliance programmes and to involve third parties in the investigation and verification processes.

Which third parties should we engage? What key performance indicator is useful? What should we report to be more credible?

**Response: Approach to transparency  
Transparency, disclosure, and collaboration**

We value transparency and stakeholder feedback. We report regularly on our compliance work including the location of our suppliers globally. We also submit our programme to evaluation, accreditation and public reporting by the Fair Labor Association. Moreover, we continue to practice full disclosure to researchers, trade unions and other concerned NGOs, based on their specific requests. In 2006, we continued in our practices to disclose factory names and addresses to several local union affiliates based on individual request. The addresses of US collegiate licensed suppliers were also disclosed to the universities in the United States that hold licensee agreements with us.

One innovative feature in our efforts to be a transparent company is the Group's participation in the Fair Factories Clearinghouse (FFC). The FFC is an industry-wide data base that centrally gathers information from the whole supply chain, and records our monitoring results. By using this data system there will be a higher level of transparency in the future: for instance, compliance information in the FFC database can be shared with other companies and third parties.

To track factory compliance performance and to support supplier selection and retention by our sourcing organisation, we are using a Key Performance Indicator.

**Working with others**

We are involved in many multi-stakeholder initiatives because we believe that working collaboratively can create lasting change in workers' conditions. In 2006 for example, we have expanded our engagement with third parties such as NGOs and government departments both at a country level and on a factory by factory basis. We engaged with other brands, local NGOs and governmental representatives to address shortcomings and failures in the application of local labour laws in El Salvador.

Throughout 2006, we continued working closely with the Fair Labor Association on the Central America project in Guatemala. This project is about developing mechanisms and tools that will produce measurable improvement of workplace conditions in El Salvador, Guatemala, and Honduras, particularly in regard to issues involving discrimination, harassment and abuse, and freedom of association

in the apparel assembly (or maquila) sector. We also worked with the FLA in bringing health care to underserved business zones outside the major cities in Honduras.

In Turkey we arranged and facilitated workshops with suppliers to improve internal monitoring skills and practices of factory compliance staff.

In 2006, the adidas Group has supported collaborative efforts to improve environmental standards by participating in the inter-brand working Group AFIRM on restricted substances as well as in the Better Cotton Initiative (BCI) targeted to enhance the environmental conditions of cotton production.

#### **Improving how we measure suppliers' performance**

After a comprehensive period of field-testing and stakeholder consultations we have begun to apply an innovative approach to measuring how well our suppliers are complying with our standards. We now measure how effective suppliers' activities are at delivering safe and fair workplace conditions through a Key Performance Indicator (KPI) introduced at a global supplier forum in April 2005. In 2007 we will extend the application of the KPI to core Reebok suppliers.

For more on this, see the Suppliers and workers section.

For more about transparency, see the Stakeholders section.

#### **Challenge: Meeting shareholder rights**

As a publicly listed company the adidas AG is obliged to fulfil defined shareholders' rights related to business information.

Shareholders and representatives of the financial community nowadays request more detailed information about the company and how the business is managing risk. Corporate reporting aids, such as the Global Reporting Initiative, have been developed to promote corporate transparency and disclosure. Increasingly, publicly listed companies are rated against transparency benchmarks.

#### **Response: Corporate Governance and risk management**

To effectively and responsibly manage risks and challenges, standards of good corporate management are important. We have established a

corporate governance framework that addresses rights of shareholders, the responsibilities and duties of the Executive Board including social and environmental considerations and the Supervisory Board and how they collaborate; information and disclosure obligations; and solutions for any conflicts of interest.

The governing principles we have established ensure good management and control of the business. A comprehensive risk management system addresses internal or external risks that may affect the Group's goals, strategies, brand image, or financial performance and health. Social and Environmental Affairs is an integral part of the risk management system and provides the Executive Board with regular updates on social and environmental risks and developments. SEA strategic business plans that have been approved by the Board supported the development of business contingency plans and staff advisories for public health issues like avian flu.

For more information on corporate governance, see the Investors section on our website.

#### **Challenge: Managing an external supply chain**

Our supply chain is large, multi-layered and complex. It comprises many different suppliers that principally can be categorised in four groups: main factories, subcontractors, material suppliers and licensees. With the addition of Reebok a further intermediary was added to our supply chain: agents.

Outsourced production is not without its risks. We have less direct control over suppliers' operations or workplace and environmental conditions at their factories than at company-owned sites.

#### **Not enough capable managers**

We have a code of conduct, our 'Workplace Standards', which guide our suppliers on achieving acceptable working conditions. Our efforts are directed at addressing the root causes of problems and helping factories to improve by developing and running their own management and governance systems. To operate and maintain these, factories need capable people who are trained, competent and experienced. Within our major sourcing countries we have found that there is a very limited supply of skilled middle managers with health & safety and human resource management skills, and where there are capable people, turnover rates are high.

### **Peak demand stretches suppliers**

Major sporting events create challenges in managing product demands and peak production loads in a limited base of suppliers. Also, marketing and promotion campaigns for major sports events often include specialty and give-away items, which are ordered through agents who operate outside of our main supply chain.

We are a successful company. And that success is measured in the demand for our products. While we strive to consolidate the supply chain for our core business and international export market production, we are entering into licensing arrangements with specialty firms, supporting investment and green field development by our existing business partners, who are building new factories, and finding new suppliers to fill orders for each local market.

### **Response: How we work with suppliers**

Our strategy is based on a long-term vision of self-governance for our suppliers and focuses on:

- supporting business partners in their efforts to establish effective human resources, health & safety and environmental management systems
- building capacity within the workforce and the management of our supply chain to ensure fair and safe working conditions
- raising environmental awareness and promoting best environmental practice, and
- expanding our interaction with local worker organisations and NGOs to better understand working conditions in places where our products are made.

We act as both inspectors and advisors, assessing management commitment to our 'Workplace Standards' but also training our suppliers on the key issues. We use a new key performance indicator to measure the effectiveness of actions taken by suppliers and we also provide training materials, such as our Sustainable Compliance guidelines, to help suppliers understand what is needed from them to achieve self-governance.

We are extending the contractual obligations of those agents and licensees who operate outside of our main supply chain to include compliance with our 'Workplace Standards'. We now require agents and licensees to develop strategic compliance plans that show how they manage their suppliers'

compliance. These plans are subject to review by the adidas Group.

For more, see the Suppliers and workers section.

### **Challenge: Being competitive and customer-focused**

Real athletes want to perform well in all conditions. The same goes for the adidas Group: we need to be flexible and to perform at our best to thrive in the highly competitive sporting goods market, with its ambitious new players, and constant product innovations.

Shorter product cycles and the demand for more individualised products are specific challenges that not only affect marketing strategies but also our sourcing models. We are also expanding into markets that are more seasonal, for example lifestyle and fashion.

Cost-effective product manufacturing and distribution are further imperatives. To remain competitive, we have outsourced production to countries where product costs are less. Interestingly, the emerging countries from which we source are themselves developing into major consumer markets for our products. The line between export producers and local or domestic manufacturers is becoming blurred.

### **Managing uncertainty**

External factors such as rising prices of energy or the end of the Multi-Fibre Arrangement (which set quotas for textile imports) require both our sourcing strategies and suppliers to be very adaptable. The transitional period, as the EU and the US governments negotiated new textile quotas, created a great deal of uncertainty in the industry.

In 2006, the Council of the European Union imposed an anti-dumping duty on imports into the EU of footwear with leather uppers originating in China and Vietnam. These anti-dumping measures will be applicable for two years. Initial discussions about potential anti-dumping duties indicated that approximately 20% of our Group's footwear volume would have been impacted. However, we began sourcing these products from Indonesia and Thailand early in 2006 because of the potential imposition of import duties. As a result, when the legislation became effective, only limited fine-tuning of our source base and product allocation was necessary to eliminate virtually all negative impacts

resulting from these duties.

Going forward, we will continue to diversify our sourcing portfolio across all product types to gradually reduce reliance on China-only sourced product. Our overall plan is to reduce the proportion of sourcing volume in China by increasing capacities in other countries such as Indonesia, Vietnam and India. In 2006, we introduced India as a new footwear sourcing country and will gradually grow capacity there in the coming years.

#### **Response: Competing responsibly**

We believe that the values and principles we share with our business partners positively impact business and the life of people making our products. We communicate these values through our 'Workplace Standards', the Group's code of conduct. The Standards are based on the International Labour Organization (ILO) and UN conventions relating to human rights and employment practices. They follow the model code of conduct of the World Federation of Sporting Goods Industry.

#### **Integrating standards**

The 'Workplace Standards' form a fundamental base of our relationships with our suppliers and are a contractual obligation. Before suppliers can become authorised business partners, they must be able to show how they comply with our Standards. But this is not the end point. We want to see our suppliers integrating the standards fully in their management and decision-making process, and finally moving towards a system of self-governance.

The results of supply chain compliance performance must inform the Group's operations team and other supply chain decision makers. The 'Workplace Standards' are an integral part of the Global Operations cumulative factory rating system and ensures that customer demands and competitive advantages are achieved in a responsible environment.

The Social and Environmental Affairs team is tasked to ensure supply chain compliance with the 'Workplace Standards' and manage wider corporate responsibility activities of the Group. The team is led by three regional Heads and the Global Director who reports to the General Counsel and the Executive Board of the Group. The SEA team collaborates closely with the Global Operations group, which is responsible for developing and sourcing products from suppliers.

For more see the Mission and values section.

#### **Challenge: Sustainable products**

Sustainability poses a number of challenges for our innovation and development teams as well as manufacturing partners. The goal is to achieve a balance between various demands: the products must not only be competitive in function and price, but also safe (during use and after disposal) as well as environmentally friendly. Manufacturing needs to be done with the least environmental impact without compromising quality.

#### **Response: Being environmentally responsible**

Reducing pollution with so-called end-of-pipe solutions offers only limited environmental benefits, so we strive to design out environmental problems by rigorously applying the following principles:

- Compliance with all legal local laws and regulations
- Apply best practices at own sites and operations
- Product materials and components to be non-toxic and safe
- Promote environmental management systems and best practices in the supply chain, where major environmental impacts occur.

Following the addition of Reebok, we reviewed all policies, procedures and practices to ensure we are operating to the highest standard. We have now made it mandatory for all our core suppliers to establish environmental management systems, which will encourage them to plan, manage and review their own environmental performance. We have harmonised the way we capture and report on resource consumption at our own factories and major sites, and have introduced similar environmental metrics for our suppliers' footwear factories. These initiatives will allow us to identify and share best practice across the whole Group – both at our own sites and in our supply chain.

For more see the Environment section.

#### **Challenge: Managing and developing our people**

Being a global player in a disparate and constantly changing world creates complex challenges with regard to the management of our employees. Our HR strategy therefore has to:

- embrace diversity as a stimulus rather than a restriction

- monitor demographic changes and respond with the appropriate recruitment and retention strategy and work-life balance initiatives
- mirror the global marketplace with a multinational workforce and, promoting mobility that complies with different local laws and incorporates cultural differences
- listen to our employees, understand their needs and motivations and help them to realise their full potential.

**Response: Making the adidas Group the place to be**

The success of the Group is a direct result of the commitment and talents of people who work for us. We want to create the best and most productive workplace in the industry by:

- creating a working environment that stimulates team spirit and passion, engagement and achievement
- instilling a performance culture, based upon strong leadership
- fostering an understanding of social and environmental responsibility for the world in which we live – for the rights of all individuals, and for the laws and customs of the countries in which we operate
- providing a secure working environment.

For more see the Employees section.

**Challenge: Supporting local communities through effective programmes**

As a multinational enterprise the adidas Group is represented in many countries around the world and its business operations impact the lives of the people in those communities. While there are many ways and possibilities to donate money and resources, the challenge is to know the local needs of the communities and to identify programmes that sustainably enhance the social and environmental infrastructure and positively impact the business environment too.

**Response: Decentralised decision-making within a global framework**

The adidas Group has adopted a largely decentralised and brand-oriented model for community involvement practices, recognising that people in our regional subsidiaries and Group entities best understand the needs and cultural sensitivities of their local communities. At the Group level we continue to support our suppliers' communities, as well as make contributions to

organisations that promote sustainable development practices within the industry.

Initiatives that derive from the brands' individual identities and value sets may vary in form, but they are all aimed at supporting children and young adults, with sports as a common theme. Our key brand community programmes are described below:

**Adi Dassler Fund**

The Fund supports organisations that connect children with coaches who teach life values in addition to sport. These organisations and their programmes use sport to teach things such as self-confidence, respect and teamwork that can break down barriers and allow people to live healthier, happier lives. The Fund receives assistance from the adidas Brand and its employees around the world.

**Reebok Human Rights Foundation**

In 2007, the Reebok Human Rights Foundation and Community Relations programme will continue financially supporting organisations in and around Reebok World Headquarters, namely the Greater Boston area. We will award grants and expand existing strategic alliances and collaborations with organisations that promote social and economic equality through programmes serving inner-city youth and underserved minority groups.

**TalorMade programme**

TaylorMade-adidas Golf is committed to supporting charitable organisations that champion youth, golf, and those less fortunate of all age groups. TMaG supports sports and community events near its head office in Carlsbad, California as well as charitable organisations in England, Korea and Japan.

For more see the Community affairs section.

**Progress**

As we aim to become a sustainable business with self-governing suppliers, we set ourselves annual targets. We have reported progress against these annual targets for six years now and see this as a crucial step in being accountable to our stakeholders. The three sections below list our targets for 2006 and describe our progress in achieving them:

- Management targets 2006
- Suppliers targets 2006
- Environment targets 2006

### Management Targets 2006

Targets 2006	Progress	%
To ensure an effective and people minded integration of the adidas and Reebok companies by managing the appointment process and the alignment of the remuneration practices.	The appointment process was concluded by April 1st, our „Go live“ date for the new integrated Group. The process was managed by an external auditing firm to ensure an “equal opportunity” approach. The ratio of adidas and Reebok employees appointed to leadership roles reflects the ratio of employees of the two companies before the merger. The integration was supported by change management processes, such as a regular pulse check that was discussed and reacted to by the management.	100
HR Talent Management/ Performance management: To implement the Group’s Talent Performance Management and Career development concepts (team line up, Champions league, PEP) in all Regions and HQ functions.	All Talent Management as well as Performance management tools and concepts are implemented and in place in the new Group. Talents from all brands and regions have participated in all modules of our Leadership programmes in 2006 and in the first quarter of 2007. This has contributed significantly to a smooth integration from a people point of view. We also launched a group wide competency model that is the backbone of all hiring, training and development efforts.	100
To unify the existing brand compliance programmes into one Group-wide function.	A Group-wide social and environmental compliance organisation was established integrating the adidas and Reebok brand programmes. Three major milestones were reached: <ul style="list-style-type: none"> <li>• Creation of a new Group-wide set of workplace standards</li> <li>• Establishment of new internal and external monitoring procedures covering initial factory assessments, and ongoing monitoring of non-compliances and their root causes</li> <li>• Factory assessments are now recorded in our central database – the Fair Factories Clearinghouse.</li> </ul>	90
To distribute the CSR survey among adidas Group employees; to analyse and report back on survey findings.	The survey was conducted among a representative number of adidas employees (prior to the acquisition of Reebok). Survey findings were shared with Senior Management and a summary report has been posted on the website.	100
To finalise the review of the Group’s internal code of ethics and to plan the rollout of a Group-wide compliance programme.	The revised adidas Group’s code of ethics was officially approved by the Executive Management and the Works Council. Rollout via eLearning tools is scheduled for 2nd half of 2007.	70
To develop a regular review mechanism of supplier compliance KPI with the Sourcing organisation.	<ul style="list-style-type: none"> <li>• The SEA compliance KPI has been incorporated as a benchmark for core suppliers; biannual updates of the KPI for a period of three years.</li> <li>• The SEA Enforcement Guideline was finalised and launched with approximately half of the Group entities.</li> <li>• All regions have at least one annual supply chain review between Global Operations, Business Units and SEA.</li> </ul>	80

### Supplier Targets 2006

Targets 2006	Progress	%
To roll out the first two modules of HR management system (HRMS) and to provide training to a selective group of key suppliers in China.	<ul style="list-style-type: none"> <li>All four pilot groups in China were kicked off and have received HRMS training in 2006.</li> <li>Participating suppliers were given assignments relating to specific HRMS improvements to implement in their respective factories, and have completed and presented their implementation plans.</li> <li>Suppliers have also submitted HRMS progress reports and outlined their future plans for HRMS implementation.</li> </ul>	100
To fully apply the new SEA compliance KPI for all key suppliers per region, update their compliance performance rating, and link the KPI to supplier strategic compliance planning and expectations for the Sustainable Compliance Guidelines.	<ul style="list-style-type: none"> <li>All key suppliers received updated KPI and compliance performance ratings.</li> <li>Approximately 15% had the KPI linked to strategic compliance planning.</li> <li>Unplanned but successful strategic compliance planning with all of the critical Reebok business units and sourcing agents.</li> </ul>	60
To fulfil our obligations towards the FLA in view of an increased number of applicable factories.	All obligations for monitoring, remediation and project work were completed.	100
To apply the safety officer registration and training programme with selected suppliers in one key sourcing country in Asia.	<ul style="list-style-type: none"> <li>Safety officer registration and training was delivered in two countries in Asia: Vietnam and Cambodia.</li> <li>Candidates registered at a level based on their academic background and work experience. There were three modules taught for each level of Safety Officer Training: <ul style="list-style-type: none"> <li>- Module 1 - Occupational Safety</li> <li>- Module 2 - Occupational Health</li> <li>- Module 3 - Safety Management</li> </ul> </li> <li>Trainees are required to pass a test paper and complete a project report for each module.</li> <li>All Safety Officers are tracked with a registration number and individually assigned a progress report card.</li> </ul>	100
To commit at least 5 worker dialogues in the Americas, Asia and Europe with focus on worker-management communications and verification of the country risk assessments.	<ul style="list-style-type: none"> <li>Dialogues with workers from factories Hermosa, Satellite and Chi Fung in El Salvador.</li> <li>FLA Central America Project II (FLA CAMP II) in Guatemala.</li> <li>Multi-stakeholder engagement in Honduras to bring health care to underserved business zones outside the major cities.</li> <li>Training of two factories in Turkey on worker-management communications.</li> <li>Workshop with 12 Turkish suppliers' internal compliance staff on internal auditing methods.</li> <li>An innovative quiz competition was held for workers in China to engage them and strengthen their understanding of health and safety in the workplace. Six factories participated.</li> <li>Extensive worker dialogues were held regarding the ongoing operation of welfare committees in five factories in China, as well as the establishment of worker-management committee in two factories in Indonesia and a factory in India.</li> </ul>	100

	<ul style="list-style-type: none"> <li>• Following large-scale factory closures in Indonesia, SEA held an intensive dialogue with workers and unions from three factories over the design of a humanitarian aid programme (medical care and job placement).</li> <li>• An Industrial Relations stakeholder dialogue also took place in Vietnam to address the increasing numbers of strikes in that country.</li> </ul>	
Increase our strategic monitoring practice to 75% of SEA factory monitoring exercises.	<ul style="list-style-type: none"> <li>• 100% of the initial SEA assessments of factories were completed using strategic monitoring methodologies.</li> <li>• 80% of factory visits resulted in an updated SEA KPI performance rating.</li> </ul>	80
Ensure that all key suppliers develop and start implementation of strategic compliance plans informed by KPI ratings.	<ul style="list-style-type: none"> <li>• 90% of our global key suppliers were developing strategic compliance plans. Already 25% of the global key suppliers had strategic compliance plans implemented.</li> <li>• 75% of key business units and sourcing agencies were developing strategic compliance plans.</li> </ul>	80

#### Environment Targets 2006

Targets 2006	Progress	%
To finalise the development of an HSE Guideline for SMEs and to identify external service providers for rollout and training.	The new guideline structure has been reviewed and field-tested in selected regions. The guidelines will be merged with the core set of HSE guidelines that are subject to complete revision following the integration of the adidas and Reebok social and environmental programmes.	30
To run energy-saving workshops for key footwear suppliers in Asia facilitated by environmental consultants.	Energy workshops scheduled for 2006 were postponed and took place in China and Vietnam in 1st quarter 2007. In addition to adidas and Reebok footwear facilities strategic suppliers from other product divisions such as apparel also participated.	90
To extend the use of the environmental indicator system to one selected footwear and vertically integrated supplier in Latin America.	The environmental indicator system was extended to core footwear suppliers and a vertically integrated supplier in Latin America, as well as to the southern region of Africa.	100
To provide a progress report on the Better Cotton project.	<ul style="list-style-type: none"> <li>• Work with regional and local groups in India and Pakistan started to prepare for training farmers.</li> <li>• BCI hired full time manager to strengthen project rollout process.</li> <li>• Extended stakeholder outreach to obtain feedback on labour issues in the cotton industry.</li> </ul>	80
To develop an environmental accounting framework for all major sites of the adidas Group.	A standard template and reporting process has been developed for recording environmental key data from major administration sites and production facilities operated by the adidas Group. After rollout this will be used from 2nd quarter 2007 onwards.	70

## Targets for 2007

In 2007 we will apply the newly integrated programme across all brands of the adidas Group for the first time. Key targets are to:

- ensure the consistent rollout of our new programme standards across the supply chain
- finalise supplementary guidance materials and strategic compliance plans for training and supportive activities with our suppliers
- finalise the Group-wide compliance data management system (FFC) so we can communicate and report on our social and environmental performance to internal and external stakeholders
- as the new unified Group, continue to fulfil our obligations as a Participating Company of the Fair Labor Association
- ensure Sourcing decisions are increasingly informed by supplier compliance Key Performance Indicator (KPI) ratings
- become the employer of choice in our industry and our target group by becoming a "world class recruiter" and by extending our "emerging employee" programmes beyond brands, functions and borders
- Talent Management/Performance management: Bring sustainability to our Group-wide programmes and monitor success, for example by conducting employee engagement surveys. Establish ourselves as a leader in Talent Management internally and externally.

## Glossary

### Capacity building

Helping our business partners and others understand how to manage and improve workplace conditions, e.g. through training, producing guidance manuals, and sharing best practice.

### Community Affairs

Corporate function which coordinates a network of employees managing corporate donations, volunteering programmes and community relations in the subsidiaries and other local entities of the adidas Group. This function has become part of the SEA team in 2005.

### Corporate Social Responsibility (CSR)

Managing a company's business processes in a way that creates economic value while also respecting

people and communities and minimising environmental impact.

### Eco-Management and Audit Scheme (EMAS)

System designed to improve a company's environmental performance by ensuring that all environmental effects and impacts of a facility are recorded and documented.

### Fair Factories Clearinghouse (FFC)

A collaborative industry effort involving retail and consumer brands and retail trade associations to create a system for managing and sharing social audit information.

### Fair Labor Association (FLA)

Non-profit organisation working cooperatively with companies, NGOs and universities, to promote a workplace code of conduct based on International Labour Organization standards.

### Flock transfer printing

Technology that allows structural and solid print designs.

### Global Operations

Board function responsible for the global development and sourcing of adidas products such as footwear, apparel, accessories and gear.

### Global Reporting Initiative (GRI)

Independent institution developing a generally accepted framework for sustainability reporting.

### Hot melt

Environmentally safe bonding technology using heat-activated adhesives.

### ISO 14000/1

Environmental management standard.

### Key Performance Indicator (KPI)

Measures the effectiveness of actions taken by our suppliers to ensure compliance with the "Workplace Standards".

### Lean

Manufacturing efficiency programme promoted by the adidas Group to improve overall factory performance in terms of delivery, quality and cost.

### Lean/6 Sigma

A more sophisticated methodology aimed at eliminating defects.

**Multi-Fibre Arrangement (MFA)**

Introduced in 1974, establishing the rules for international trade in textiles and garments. Through the MFA, quotas were set limiting the amount of imports of textiles and clothing to the developed world. The MFA expired at the end of 2004.

**Non-Governmental Organisations (NGOs)**

Special interest groups, often not-for-profit, raising awareness of sustainable development issues in business.

**Occupational Health and Safety Assessment Series 18001 (OHSAS)**

Occupational health and safety standard.

**Polyvinyl chloride (PVC)**

Synthetic material used in the manufacture of sports apparel and hardware that we are striving to phase out because of its adverse health and environmental impacts.

**Social and Environmental Affairs (SEA)**

Department of the adidas Group responsible for producing and developing sustainability policies and initiatives, and promoting social and environmental awareness throughout the company and its supply chain.

**Socially Responsible Investment (SRI)**

Investment that is made on the basis of the financial, environmental and social performance of a company.

**Stakeholder**

Person, community or organisation that affects, or is affected by, the operations of a company.

**Standards of Engagement (SOE)**

The SOE have been replaced by the adidas Group's 'Workplace Standards' as of 1st January 2007. Please see 'Workplace Standards' for explanation.

**Sustainability**

The ability to create economic, social and environmental value in the long term.

**Volatile Organic Compounds (VOCs)**

Solvents that can cause breathing and health problems. VOCs are by-products of the shoe manufacturing process.

**Workplace Standards**

The Group's supply chain code of conduct, formerly known as the 'Standards of Engagement' (SOE). A set of labour, health and safety, and environmental principles designed as tools to help the adidas Group choose supply chain partners, monitor their performance and identify problems.

## WORKPLACE STANDARDS

### **Performance. Passion. Integrity. Diversity.**

These are the core values found in sport. Sport is the soul of the adidas Group. We measure ourselves by these values, and we measure our business partners in the same way.

Consistent with these values, we expect our partners – contractors, subcontractors, suppliers, and others – to conduct themselves with the utmost fairness, honesty and responsibility in all aspects of their business.

We use the adidas Group Workplace Standards as a tool to assist us in selecting and retaining business partners who follow business practices consistent with our policies and values. As a set of guiding principles, the Workplace Standards also help identify potential problems so that we can work with our business partners to address issues of concern as they arise. Business partners will develop and implement action plans for continuous improvement in factory working conditions. Progress against these plans will be monitored by the business partners themselves, our internal monitoring team and external independent monitors.

Specifically, we expect our business partners to operate work places where the following standards and practices are implemented:

### **General Principle**

Business partners must comply fully with all legal requirements relevant to the conduct of their businesses.

### **Employment Standards**

#### **Forced Labour**

Business partners must not use forced labour, whether in the form of prison labour, indentured labour, bonded labour or otherwise. No employee may be compelled to work through force or intimidation of any form, or as a means of political coercion or as punishment for holding or expressing political views.

#### **Child Labour**

Business partners must not employ children who are less than 15 years old, or less than the age for completing compulsory education in the country of manufacture where such age is higher than 15.

#### **Discrimination**

Business partners must not discriminate in recruitment and employment practices. Decisions about hiring, salary, benefits, training opportunities, work assignments, advancement, discipline and termination must be based solely on ability to perform the job, rather than on the basis of personal characteristics or beliefs, such as race, national origin, gender, religion, age, disability, marital status, parental status, association membership, sexual orientation or political opinion. Additionally, business partners must implement effective measures to protect migrant employees against any form of discrimination and to provide appropriate support services that reflect their special status.

#### **Wages & Benefits**

Wages must equal or exceed the minimum wage required by law or the prevailing industry wage, whichever is higher, and legally mandated benefits must be provided. In addition to compensation for regular working hours, employees must be compensated for overtime hours at the rate legally required in the country of manufacture or, in those countries where such laws do not exist, at a rate exceeding the regular hourly compensation rate.

Wages are essential for meeting the basic needs of employees and reasonable savings and expenditure. We seek business partners who progressively raise employee living standards through improved wage systems, benefits, welfare programmes and other services, which enhance quality of life.

### **Working Hours**

Employees must not be required, except in extraordinary circumstances, to work more than 60 hours per week including overtime or the local legal requirement, whichever is less. Employees must be allowed at least 24 consecutive hours rest within every seven-day period, and must receive paid annual leave.

### **Freedom of Association & Collective Bargaining**

Business partners must recognise and respect the right of employees to join and organise associations of their own choosing and to bargain collectively. Business partners must develop and fully implement mechanisms for resolving industrial disputes, including employee grievances, and ensure effective communication with employees and their representatives.

### **Disciplinary Practices**

Employees must be treated with respect and dignity. No employee may be subjected to any physical, sexual, psychological or verbal harassment or abuse, or to fines or penalties as a disciplinary measure.

Business partners must publicise and enforce a non-retaliation policy that permits factory employees to express their concerns about workplace conditions directly to factory management or to us without fear of retribution or losing their jobs.

### **Health & Safety**

A safe and hygienic working environment must be provided, and occupational health and safety practices which prevent accidents and injury must be promoted. This includes protection from fire, accidents and toxic substances. Lighting, heating and ventilation systems must be adequate. Employees must have access at all times to sanitary facilities which should be adequate and clean. Business partners must have health and safety policies which are clearly communicated to employees. Where residential facilities are provided to employees, the same standards apply.

### **Environmental Requirements**

Business partners must make progressive improvement in environmental performance in their own operations and require the same of their partners, suppliers and subcontractors. This includes: integrating principles of sustainability into business decisions; responsible use of natural resources; adoption of cleaner production and pollution prevention measures; and designing and developing products, materials and technologies according to the principles of sustainability.

## MISSION AND VALUES

We are striving to be the global leader in the sporting goods industry and this demands that we return strong financial results. But leadership is not only about results, it is also about how success is achieved.

We are accountable for the way we do business. In particular, we accept responsibility for the way our products are manufactured by our suppliers. By our actions we can – and should – improve the lives of workers who make our products.

Our vision is for everyone in the Group and the supply chain to share a common set of values and to follow responsible business practices. As well as improving working conditions in suppliers' factories, being responsible also means:

- Reducing the environmental impacts of our operations
- Caring for the welfare and development of our employees
- Making a positive difference to people in the communities where we operate.

In this section we list our values, our sustainability principles and our corporate missions on social and environmental affairs, human resources management and community affairs.

### Our Values

#### **Performance Passion Integrity Diversity**

These core values define who we are and what we strive to be each day: an honest and ethical business that harnesses people's different ideas and strengths, and inspired by our passion for sport, creates high performance sports goods.

### Sustainability Principles

Our core values inform our principles of sustainability, which help us set standards for our social and environmental performance. They are:

#### **Legislation**

We adhere to social and environmental laws, directives and guidelines while continually improving upon our own contribution to a sustainable society.

#### **Management**

We aim to:

- analyse, evaluate and assess the social and environmental impact of new products, technologies and processes at the design and development stage
- set up clear targets, formulate an action plan and monitor progress
- publish the results.

#### **Supplier and customer relationships**

We expect suppliers' activities to be compatible with our 'Workplace Standards'. We work in partnership with them to improve our collective performance. We encourage our business customers to take a proactive stance on the social and environmental impact of their own activities.

#### **Support**

We support social and environmental projects and develop partnerships with businesses and organisations whose direct and indirect output contributes to a sustainable society.

### **Stakeholder dialogue**

We aim to listen, respond and interact with all stakeholders in an atmosphere of mutual trust and respect. We provide them with appropriate information related to the social and environmental performance of the Group on a regular basis.

### **Corporate Missions**

Our principles of sustainability outline the operational framework for becoming a more sustainable company, and inform our individual missions in Social and Environmental Affairs, Human Resources management and Community Affairs.

#### **Mission for Social and Environmental Affairs**

Being a leader in terms of social and environmental affairs means we are dedicated to socially responsible, safe and environmentally sustainable practices in the Group and its supply chain, and to enhancing the value of our brands by:

- guaranteeing the ideals of the company for the consumer and for those making our products
- making the supply chain more effective
- strengthening our image and reputation
- helping to provide a long-term future for sport.

#### **Mission for Human Resources**

The success of the Group is a direct result of the commitment and talents of people who work for us. We are seeking to build the leading global team in the industry.

Our mission is to create the best and most productive workplace in the world by:

- creating a working environment that stimulates team spirit and passion, engagement and achievement
- instilling a performance culture, based upon strong leadership, setting the ground for winners
- fostering an understanding of social and environmental responsibility for the world in which we live; for the rights of all individuals, and for the laws and customs of the countries in which we operate
- providing a secure working environment.

#### **Mission for Community Affairs**

It is our responsibility as a member of each community to act as a true corporate citizen and we are committed to doing this through a range of

activities including corporate giving, volunteer work and community relations programmes.

### **Social and Environmental Affairs Team**

The Social and Environmental Affairs (SEA) team is tasked with ensuring the Group is working towards its vision to operate responsibly. In practice, this means the team ensures compliance with our 'Workplace Standards' within the supply chain and manages the Group's environmental and community affairs programme.

The SEA team consists of a diverse group of 62 individuals – engineers, lawyers, HR managers, and former members of non-governmental organisations (NGOs). The group is organised into three regional teams covering Asia, the Americas and Europe, Middle East and Africa (EMEA).

#### **How the SEA team works**

SEA collaborates closely with other global functions such as Sourcing, Legal, Marketing, Product Development, Facility Management and HR. It is directly involved in developing and updating corporate policies and operating procedures related to social accountability, product safety and compliance with environmental laws and regulations.

The collaboration with Sourcing has been particularly important for improving workplace conditions in the adidas Group supply chain. Over the years, SEA has established collaborative systems and processes to ensure Sourcing fully consider compliance with workplace standards. All potential new suppliers have to undergo an initial assessment performed by the SEA team and orders can only be placed with SEA's approval. And monitoring information gathered by the SEA team is regularly shared with Sourcing so they are aware of the latest compliance status of each supplier.

By engaging directly with suppliers, government and other external stakeholders, SEA is informed about social and environmental issues at an early stage. It addresses any potential risks, and health, safety and environmental liabilities, in its monthly report to the Executive Board and Sourcing Management.

The SEA team follows a rolling three-year strategy that focuses on how our sustainability principles and missions can be integrated into our day-to-day operations and work with business partners.

This strategy, together with our business principles and the results of regular interaction with stakeholders, forms the basis of our road map to sustainability. This is outlined below:

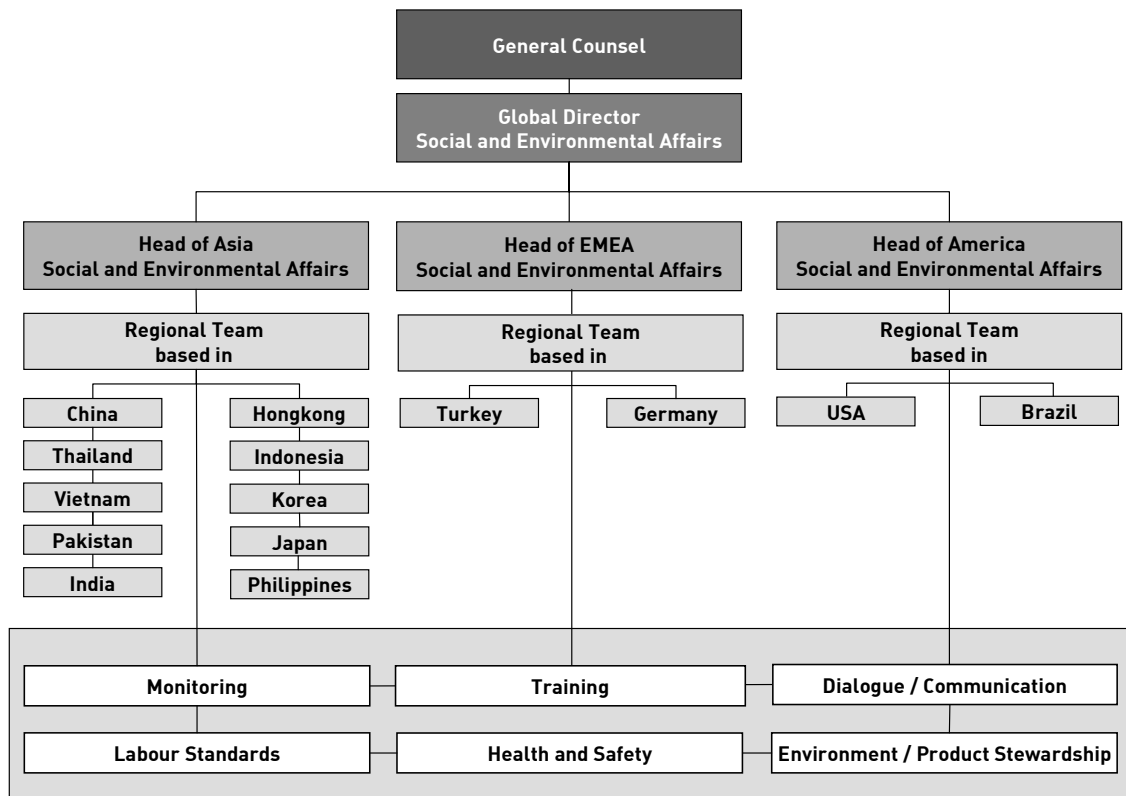
1. Supporting business partners in developing effective human resources and health, safety and environmental management practices in their manufacturing operations.
2. Building capacity within the workforce and the management of our supply chain so they understand how to manage and improve workplace conditions themselves.

3. Expanding our network of local workers' organisations, NGOs and other representative groups so that we better understand working conditions in the places where our products are made.

4. Raising environmental awareness and promoting environmental best practice.

5. Supporting business partners in their local community activities.

Every year we determine how we will follow this road map by translating our strategic objectives into specific initiatives in the SEA team's annual action plan. Progress is measured at fixed review dates and results are reported to the Executive Board.



## STAKEHOLDERS

Our stakeholders are those people or organisations who affect, or are affected by, our operations. Companies do not operate in isolation from society and our stakeholders have a legitimate interest in the way we do business.

By involving stakeholders in key decisions that shape day-to-day operations, we gain an understanding of current and emerging issues and can best balance interests and improve our performance. We recognise that clear, effective and honest communications with our stakeholders enhances the transparency of our business and demonstrates our commitment to being accountable.

In short, actively engaging our stakeholders underpins all our efforts to be a more sustainable company.

In this section we list our stakeholders, outline partnerships we have with particular organisations and describe how we engage with our stakeholders. Two case studies highlight how we are engaging stakeholders in our supply chain.

### Our Stakeholders

Our stakeholders are a diverse group and include the following:

**Employees** of the adidas Group

**Authorisers** government, trade associations, shareholders, Board of Directors

**Business partners** unions, suppliers, service providers

**Workers** in our suppliers' factories

**Opinion formers** journalists, community members, special interest groups

**Customers** professional sports people, distributors, retailers, consumers

- Fair Labor Association (FLA)
- Fair Factories Clearinghouse (FFC)
- Environmental Consultancies
- The World Business Council for Sustainable Development
- Round table on codes of conduct, Germany
- AFIRM Working Group
- Better Cotton Initiative

### World Federation of the Sporting Goods Industry (WFSGI)

The World Federation of the Sporting Goods Industry (WFSGI) is an independent association formed by the industry suppliers, national organisations and sporting goods industry related businesses. The WFSGI enables the sports industry (including manufacturers from developing countries as well as brands based in the richer market countries) to work together on social and environmental issues.

One of WFSGI's earliest project initiatives was to phase out underage workers from football stitching. The project, which began in 1997, worked through the support of a number of different organisations, including adidas, local NGOs, the International Labour Organization, Save the Children and UNICEF. WFSGI continues to be actively involved in supporting institutional development in Asia and through its CSR Committee has extended its work

### Partnerships

We have always worked closely with our business stakeholders - including customers, suppliers, shareholders and staff - in order to build trusting commercial relationships. Increasingly, we are working in partnerships with NGOs so that together we can address their concerns about the way that we conduct our business. Noteworthy partnerships include:

- World Federation of the Sporting Goods Industry (WFSGI)

on a range of social and environmental issues that are of importance to the sports goods industry. The adidas Group remains an active member of the WFSGI's CSR Committee.

#### **Fair Labor Association**

The Fair Labor Association (FLA) is a non-profit organisation made up of private corporations, non-governmental organisations and universities. It sets workplace standards and appoints accredited inspectors to monitor how well affiliated companies meet these standards. The FLA publishes an annual report with each company's results. The FLA accredited the Reebok and adidas programmes in 2004 and 2005. As part of the 2006 obligations, adidas and Reebok received 43 independent, external monitoring and verification visits from FLA monitors, and these tracking reports can be found on the FLA's website. Both brands are active participants in FLA activities, including sustainability assessment (FLA 3.0), annual reporting, and best practice training for suppliers.

In 2007, the adidas Group, including the adidas and Reebok brands, will assume the role of an FLA participating Group. This means the FLA will evaluate the SEA programme as an integrated entity operating under a single management team, with a single but enhanced set of policies and practice. The next FLA evaluation and programme re-accreditation is scheduled for 2008.

#### **Fair Factories Clearinghouse (FFC)**

The Fair Factories Clearinghouse (FFC) is a US-based non-profit corporation founded in 2004 and funded by member contributions and a grant from the U.S. Department of State, Bureau of Democracy Human Rights and Labor.

Reebok was a founding member and has been instrumental in the development of the organisation, which houses a global database of factory information and social compliance audit reports. The database enables member companies to manage and share non-competitive information about workplace conditions to help promote factory improvement. Following the integration of adidas and Reebok in 2006, the FFC has become the Group's primary factory compliance tracking system.

For further information, see [www.fairfactories.org](http://www.fairfactories.org).

#### **Environmental consultancy INTECHNICA**

INTECHNICA are environmental and management consultants who help the adidas Group to introduce and maintain management systems for occupational health, safety and environmental protection and assist in establishing and developing quality management systems at various sites of the Group.

INTECHNICA is part of an international network with locations in London, Brussels, Pamplona and Singapore.

#### **The World Business Council for Sustainable Development (WBCSD)**

The membership of the adidas Group in the World Business Council for Sustainable Development (WBCSD) was agreed in 2000 and became effective in January 2001. The Council is a coalition of some 200 international companies who share a commitment to sustainable development.

The WBCSD aims to develop closer co-operation between business, government and all other organisations concerned with the environment and sustainable development, and to encourage high standards of environmental management in business.

We aim, through the Council, to share our experiences with other companies and stakeholders and to extend our knowledge of issues relating to sustainability. The adidas Group has been engaged in various working Groups over the last 5 years and contributed to guidance materials about sustainable development and CSR issued by WBCSD to its members.

#### **Round Table on codes of conduct, Germany**

We are participating in a Round Table on codes of conduct established and facilitated by the German Ministry for economic development and cooperation. The Round Table comprises representatives of the private sector, trade unions, non-governmental organisations and government.

The objective of the Round Table Codes of Conduct is to improve the implementation of labour and social standards in developing countries through corporate codes of conduct.

Working together, the Round Table is focusing on designing effective and universally acceptable processes for the introduction, monitoring and verification of voluntary codes of conduct. This

includes how to adequately involve trade unions/ employee representatives and non-governmental organisations.

#### **Project involvement**

The adidas Group is engaged in a project that was developed by a sub-working group of the Round Table. The project is about improving working conditions and competitiveness in subcontractors to multinational companies in Romania, by providing training on in-company dialogue between management and employees.

The project began in February 2005 and ran through until October 2006. Through effective training, the project enhanced communication and negotiation skills among the workforce and the management of the participating factories. This in turn fostered improvements in industrial relationships and social dialogue.

Some participating factories elected worker councils and implemented formalised official dialogue structures or official grievance systems. Both management and workers had the chance to become more aware about each other's problems, which has helped to increase transparency in many of the participating companies. Various suppliers reported that productivity has increased and as a result overtime was reduced; some implemented incentive systems or even raised wages. Some suppliers also started to informally co-operate in various areas such as material logistics or package service.

Read more at [www.coc-runder-tisch.de](http://www.coc-runder-tisch.de).

#### **AFIRM Working Group**

The adidas Group is an active member in The Apparel and Footwear International Restricted Substances (RS) Management Working Group (AFIRM). It is a multi-company working Group which provides a forum to advance the global management of restricted substances in apparel and footwear and to exchange ideas for improving RS management to ultimately increase consumer satisfaction. The AFIRM Working Group brings together product chemistry, safety, regulatory, and other experts within the apparel and footwear industry.

In 2006, the members of the AFIRM Group intensified their collaboration and information exchange and extended their scope of activities to

broader environmental issues in the companies' supply chains. The AFIRM group provided lessons on best environmental practices and restricted substances management during international textile and apparel exhibitions in Asia.

#### **Better Cotton Initiative**

The adidas Group is part of the Better Cotton Initiative, which promotes a more sustainable approach to growing cotton. The initiative aims to do this by training farmers to change their practices, and in particular to curb excessive water use, the biggest environmental issue associated with growing cotton.

In 2006, the initiative hired a fulltime project manager, consulted with various interest groups and set up the test phase of the field work.

Please find more information about sustainable cotton in the Environment section.

#### **Ways we engage**

We engage with our stakeholders in a number of ways:

- Formal stakeholder consultation meetings (called 'stakeholder dialogues') with workers, union representatives, NGOs and factory managers. See Reports of stakeholder dialogue meetings in the Stakeholder chapter of our website.
- Meetings with socially responsible investment (SRI) analysts
- With our employees through internal reporting and induction programmes
- Responding to enquiries from consumers and the media
- Collaborating with other brands in joint initiatives.

#### **SRI Fund managers and analysts**

Interest from the financial community has steadily increased. Over the course of 2006 we responded to 19 comprehensive enquiries from socially responsible investors, fund managers and financial analysts. The questionnaires they send us each require about 8-10 hours of work to complete. We also gave four telephone interviews to SRI organisations from Europe and the United States. Major subject of the interviews were the steps taken by the adidas Group to integrate the social and

environmental programmes of adidas and Reebok into one Group function.

### Employee engagement

In order to understand our employees' views on Corporate Responsibility and for adidas Group staff to better understand the work of SEA, we undertook the following initiatives in 2006:

#### Internal reporting

adidas is the world's leading football brand. To celebrate the World Cup our 2006 social and environmental report adopted the theme 'Connected by Football'. As in previous years, the report was again communicated to all our employees via our global electronic newsletters and our intranet. Furthermore, information about our social and environmental programme was distributed to all employees via the quarterly newsletter 'Inside'.

Programme updates were regularly reported via the company's newsletter and circulated to the global workforce. The Employees' newsletter also contains a new section about community affairs that provides employees with current information.

#### Employee Feedback Survey

A survey was conducted on the importance of various aspects of corporate responsibility to our employees and the support provided by the SEA team. A summary of survey findings can be found in the Stakeholder section of our website.

#### Induction of new employees

In Asia, approximately 100 new managers and staff were provided with an orientation session on the social and environmental affairs programme. For about 90 new employees in North America, an annual HR orientation was conducted, including a history of the social and environmental programme. In Europe 198 new employees participated in five orientation sessions on SEA in the adidas Group's Headquarters in Herzogenaurach, Germany.

#### Training provided to employees of the adidas Group

The following training sessions took place:

- Americas – there were 18 training sessions for 74 employees of the adidas Group, including integrated SEA policy briefings and FFC training.
- Europe – SEA team members held 6 training sessions for a total of 49 adidas employees from Turkey, France, Germany, Italy and UK.

This includes one orientation session on SEA for 14 new employees in Turkey.

- In Asia, the SEA team provided 24 training sessions for internal staff in China (Guangzhou, Shanghai and Hong Kong), India, Indonesia, Japan, Korea, Malaysia, Philippines, Thailand and Vietnam. This includes two cross-training sessions on compliance for TaylorMade and the Hockey Company sourcing staff from North America.

### Responding to enquiries

#### Customers

In 2006, we responded to each inquiry, whether they were submitted by individual consumers, academics, school classes or retailers. Major subjects of inquiries were:

- the production of footballs with regard to the 2006 FIFA World Cup in Germany
- product safety – adidas Group policy on restricted substances
- environmental issues – adidas Group programme on the elimination of PVC
- the company's supplier monitoring programme
- the integration of the social and environmental programmes of adidas and Reebok
- specific supplier cases.

#### Media

We had a high level of media activity during 2006, with the FIFA World Cup™ hosted in Germany. Through the course of 2006, we received more than 43 formal enquiries from the media – the international press, radio and television. This included 27 requests for interviews. On 14 occasions, journalists visited factories and were accompanied by SEA staff. The majority of these visits were to Molten Thailand, where the adidas World Cup ball was being manufactured. One visit was declined and one visit deferred to 2007. The Social & Environmental Report 2006 was made available to the media and journalists' questions were discussed upon request.

#### Non-Government Organisations

NGOs, worker rights groups, campaigners, students and the academic community were active through the year, raising questions and presenting proposals regarding workplace conditions. Examples of enquiries include:

- questions over supply chain transparency and whether adidas will make public the names and addresses of our suppliers' factories

- the impacts arising from the integration of the Reebok supply chain, following the acquisition of this brand
- the reinstatement of workers dismissed by PT Panarub, a supplier being independently monitored by the Worker Rights Consortium (WRC)
- repeated allegations by an NGO concerning the closure of garment factories in El Salvador (Hermosa and Chi Fung) and in Honduras (BJ&B)
- the end of the Multi-Fibre Arrangement and the Group's sourcing strategies
- NGO concerns related to the closure of three Reebok footwear suppliers in Indonesia, which resulted in large scale layoffs and worker protests
- a proposal from United Students Against Sweatshops (USAS) to require university logo apparel goods to be produced by designated suppliers where workers earn a living wage and are represented by legitimate trade unions.
- BDA (German Employer Association) ad hoc Working Group on CSR.  
See [www.csrgermany.de](http://www.csrgermany.de)
- 'Stiftung Warentest' football testing (Germany)
- Liaison with International Toys Confederation and various toys manufacturer to discuss common standards
- CSR Forum in Beijing hosted by Ministry of Commerce and UN Global Compact
- Engagement with FIFA on community initiatives for World Cup 2010
- Panel discussion on globalisation and fair trade organised by the community of Herzogenaurach, Germany, where the adidas Group is headquartered
- Discussions with Students Network on Sustainability (OIKOS) on future scientific cooperation
- Dialogue with WRC, USAS and the Designated Supplier Programme applicable to US collegiate licensed product
- Rollout of ILO-run Factory Improvement Projects in India and Vietnam
- Footwear Distributors and Retailers of America China workshop
- US National Retail Federation and FFC discussions on technology solutions and information sharing
- Discussions with Center for Reflection, Education and Action (CREA) for launching a Fair Wage Study in El Salvador
- Forum on Supplier Relocation and Impact on Workers run by Thai Center for Labor Rights
- Engagement with the Honduran Government on medical coverage and health care facilities rural for apparel workers
- Dialogue with the US Department of Labor and the US State Department over legal and trade issues in EL Salvador
- Formation of a Better Workplace Association in Beijing, to support education and awareness raising in China in relation to labour rights and occupational health and safety
- Participation in Levis-run brand collaboration meetings for the apparel sector
- Feedback to Dutch Ministry of Economic Affairs on the effectiveness of OECD complaint mechanisms
- Marie Stopes International and Concepcion Caceres Women's health project in Honduras
- CSR Community initiative in Guangzhou/China
- Ongoing dialogue with Play Fair Campaigners and Oxfam International on 'Offside' report

Our public responses to these concerns can be found in our Statements section on the website.

### Participation and collaboration

In 2006, the adidas Group actively participated in the work of the World Business Council for Sustainable Development, the World Federation of Sporting Goods Industry's CSR Committee and the Fair Labor Association.

We also participated in:

- Discussions with the Global Business Coalition on HIV/AIDS China Working Group regarding HIV/AIDS programmes being implemented with Marie Stopes International in China
- A Multi-Stakeholder Initiative pilot project (Jo-In Project) in Turkey about workplace standards; together with six international organisations, nine brands, 14 suppliers' factories and various other stakeholders.  
See [www.jo-in.org](http://www.jo-in.org)
- Multi-stakeholder engagements by the ILO Cambodia regarding the Better Factories initiative
- European Chamber of Commerce CSR Working Group in Beijing and their Supply Chain Task Force
- German Round Table Codes of Conduct; Worker-Management Communications Pilot in Romania

- International Textile Garment and Leather Workers Federation forums in the Philippines and Thailand
- ILO-US Department of Labor Industrial Relations Project, Vietnam
- Panel discussion on worker representation in China, hosted by Hong Kong NGOs and trade unions and the Trade Union Solidarity Centre of Finland
- Collaboration with WWF on CO2 offset projects
- CSC9000T, China's first indigenous social compliance standard being piloted in the apparel sector. We contributed to training on social responsibility run by CSC9000T staff and the WTO in Southern China
- General Electrics (GE) stakeholder dialogue in Asia.

In some cases we have not been a direct participant but nevertheless we have considered the outcomes and recommendations of other key multi-stakeholder initiatives and, where appropriate, we have incorporated these to our own practices and programmes. For example, Levis has developed a useful collaborative programme for shared suppliers and is working closely with a number of major brands which share a common supply chain. Although there is very little overlap between the adidas Group suppliers and Levis we believe that their collaborative approach is a useful one and should be considered as a model when entering in joint-initiatives with other brands.

## Complaint and redress mechanism

### Worker complaints and requests

In 2005 and 2006, labour rights groups, trade union officials and workers approached SEA on more than 700 occasions, seeking help or redress to issues in partner factories. The most common complaints related to strikes and disputes, unfair dismissal, discrimination, incorrect payment of wages and benefits, harassment and intimidation, excessive overtime, disciplinary practices and poor workplace conditions. Where there was an allegation or complaint, an investigation was conducted, the facts behind the case established and, where proven, action was taken.

### Improving the complaints and redress mechanism

We have strengthened the transparency of our complaints and redress mechanism by taking the following steps:

- Our complaint and redress mechanism has been incorporated in the Contact section of our website.
- The Contact section also includes a link to the FLA third party complaints channel.
- For the complaints and redress mechanism to be truly useful, we recognise that we should 'close the loop' and include worker feedback when we are commissioning new projects.

## Case studies

In this section we detail two case studies of stakeholder dialogues we have held with partners in our supply chain:

- Workers' feedback 2004
- PT Panarub factory – addressing stakeholder concerns 2002-2004

### Workers' feedback 2004

One challenge we faced in 2004 was to find ways to get clear input from workers about the effectiveness of Codes of Conduct (CoC) and compliance programmes, in a manner that maintains worker confidentiality and trust. Feedback from this key stakeholder group is critical to verifying that our compliance activities in factories are relevant and meaningful to workers.

The objectives of the engagement project were to organise the activity at a venue comfortable for the workers, to identify the gaps in their understanding of the CoC, and to develop more effective compliance and remediation tools. We also wanted feedback on how factories' compliance management systems could better address non-compliance, including management-worker communication, freedom of association, and blacklisting.

### Two worker dialogues

Two worker dialogues were held in El Salvador and Honduras in September 2004. We learned that there is a need for additional training of workers and managers to raise awareness of the CoC and local laws. Worker feedback stressed that remediation should encourage suppliers to internalise compliance programmes because there are benefits to maintaining good working conditions. Unannounced visits by auditors would encourage factories to assimilate CoC systematically and with sustainable impact rather than just cleaning up for the monitors.

### **Local facilitators**

The facilitators were NGOs local to each country – Grupo de Monitoreo Independiente de El Salvador and Equipo de Monitoreo Independiente de Honduras. They were responsible for creating the agenda, selecting participants, coordinating logistics, and producing a summary report. Representatives from organised labour, local NGOs, and the adidas SEA team attended as observers. Each dialogue included approximately 16 worker participants from local apparel factories.

### **Findings**

The dialogue facilitators agreed in the project summaries that worker engagement is essential since it enables factory workers to express their point of view about how the CoC are being implemented, and what effect the compliance programmes are having. They concluded the effort truly influences the improvement of labour practices in their supply chain.

‘Worker engagement is essential since it enables factory workers to express their point of view about what effect compliance programmes are having.’  
Summary report of worker dialogues

### **PT Panarub factory – addressing stakeholder concerns 2002-2004**

For the past five years, PT Panarub, a key footwear supplier to adidas located in Indonesia, had been beset with industrial relations problems and breaches of the SOE.

### **History of the complaint**

These issues were reported by Oxfam Australia in “We are Not Machines”, a report published in March 2002. Citing the findings of the Oxfam report, in September 2002, the Clean Clothes Campaign lodged a complaint with the Organisation for Economic Corporation and Development’s (OECDs) national contact point in Austria related to PT Panarub and another Indonesian footwear supplier, Pou Chen. The complaint was subsequently

transferred to the OECD national contact point at the Federal Ministry of Economics and Labour in Germany, for mediation. A concluding statement was issued by the Ministry in May 2004.

### **Reaching agreement**

Since 2001, the adidas Group has maintained a dialogue with Oxfam Australia and in February 2004 an agreement was reached to allow a credible and independent third party, the Worker Rights Consortium (WRC), to enter PT Panarub and investigate SOE violations. A key driver to the agreement was the acceptance by all parties of the need for greater transparency, to establish root causes and bring about lasting change. A pre-condition of the WRC’s involvement was the right to make public its findings. ‘The Assessment Team concluded that factory management illegally terminated workers’ contracts and used coercive means to compel workers to resign.’ from Worker Rights Consortium Assessment re PT Panarub (Indonesia) – Summary of findings and recommendations, September 7, 2004, page 16

### **The supplier’s response**

PT Panarub has responded positively to the findings of the WRC report, and has made improvements – the most significant of which was the restatement of previously dismissed workers and the introduction of medical insurance for all workers and their families. Despite these changes management-union relations remain problematic; in October 2004, a bonus pay dispute led to a strike and the temporary closure of the factory. To further support transparency, at the end of 2004 we began to publish updates of the ongoing remediation efforts at PT Panarub.

For an update on more recent issues at PT Panarub and the responses of the adidas Group, please see the company correspondence and statements posted in 2006 and 2007 in the Statements section of our website.

## SUPPLIERS AND WORKERS

Workers in our suppliers' factories are at the heart of our programme. It was concern for their working conditions that led us to write our 'Workplace Standards'. Some of the most challenging issues facing workers are discussed in the exploring labour standards section. Our suppliers must also safeguard their workers' health and safety. To explain how we expect our suppliers to live up to our Standards, we have produced a number of supporting guidelines that further define expectations for fair, healthy and safe workplace conditions.

Our supply chain is large, multi-tiered and varied. We have a detailed approach to managing the relationships with our suppliers and we continue to develop approaches for engaging suppliers who are part of indirect sourcing models. Monitoring compliance is carried out by the adidas Group SEA staff and commissioned third party experts while independent auditors verify compliance or evaluate our 'Workplace Standards' programmatic activities. We are committed to facilitating workplace improvement and working with others to achieve this, so we continue to invest in capacity building and outreach. We have a process for enforcing compliance with our standards and an innovative system for rating suppliers. The section case studies serves as examples of how we support supply chain activities that improve compliance performance.

### Exploring labour standards

All companies that source from developing countries face challenges in implementing codes of conduct. The adidas Group 'Workplace Standards' set out the Group's position on a number of important labour issues. In some cases implementing these standards has been particularly challenging. Here we explore the steps we have taken to meet these challenges and what we have achieved on:

- Working hours
- Fair wages
- Freedom of association
- Our position on child labour

#### Working hours

In 2002, working with the Group's Sourcing department, we surveyed Asian footwear factories on working hours. We found that, while the trend was toward reduced working hours, there were still many instances of people working more than our 'Workplace Standards' maximum of 60 hours per week.

We established a taskforce that first looked at supply-side issues and found the causes of excessive working hours included:

- poor production planning
- late material deliveries
- high turnover rates
- worker seasonality.

In 2003, the taskforce looked at internal operations at the adidas Group reviewing where we were putting pressure on the number of hours worked. The task force submitted recommendations that covered:

- a revised method of calculating main supplier production capacity, order forecasting and capacity loading
- monitoring the quality and delivery performance of raw material suppliers
- guidelines for last minute order fulfilment demands and charges.

#### Striking the balance since 2003

Despite this valuable work, the demands of our consumers for short lead times at competitive pricing have made it challenging to enforce the 60-

hour work week. Our efforts to alleviate the issue with a production efficiency drive has, in some cases, led to less overtime and less pay or even layoffs. In other cases production efficiencies have led to more secure employment – depending on how they are implemented by management.

The number of variables involved – external market demands, pricing, material suppliers' performance, staff turnover, management approach – means striking the balance between ensuring that workers consistently earn a fair wage but avoid excessive working hours.

We will continue in our efforts to drive transparency about working hours through a rigid reporting and approval system but also by supporting our suppliers in developing more efficient production and planning systems.

### Fair Wages

What is a sufficient wage to cover basic needs and reasonable savings and expenditure?

To begin investigating this question, we commissioned an NGO to carry out a pilot project on fair wages in Indonesia. Their findings were presented in a suite of reports at two workshops in 2003 in Indonesia and the USA. Read the full text of the reports on our website.

The Indonesian workshop was an opportunity to hear from a range of stakeholders and based on that and the reports, we have been able to outline a strategy to improve wages and benefits.

### Fair wage strategy

We have been working with our strategic business partners to promote a wage-setting mechanism that:

- is transparent and has the direct input by the workers, ideally through negotiation or collective bargaining, or through alternative legal means, such as a workers council or welfare committee
- benchmarks basic pay at a level that is higher than the local minimum wage
- acknowledges and rewards workers for productivity gains
- includes and takes into account data on general cost of living and workers' needs
- is part of a broader and much improved human resources management system
- meets in full all legally mandated benefits

- where practicable, promotes and supports the development of worker cooperatives.

### Freedom of association

We believe that worker-management communication is vital for successful businesses. Workers must have effective communication channels with management to help resolve workplace issues and disputes.

In order to provide clearer guidance and a deeper understanding of these requirements, we give suppliers the Guidelines on Employment Standards. The Guidelines include a dedicated section on FOA and collective bargaining and set out our expectations, case studies and practical activities to achieve compliance.

One form worker-management dialogue takes is through a trade union. While we stand neither pro nor anti-union, we believe that workers' rights to freely associate must be protected, and they must not suffer because of any union affiliation. We have persuaded factories to rehire staff dismissed for attempting to form associations (see Case study: PT Panarub – addressing stakeholder concerns).

As a buyer and third party we cannot become directly involved in forming factory associations, but we feel they have a valuable role to play in giving workers a voice and providing training on workplace safety. We are also aware that freedom of association (FOA) is a contentious issue in some countries so our approach focuses on:

- gaining a clear picture of the local political and regulatory environment for FOA in the countries where we operate
- developing individual country strategies as appropriate for promoting management-worker-union collaborations that will resolve workplace issues in a sustainable manner.

We have tried different strategic approaches in various sourcing countries like El Salvador, Indonesia, Thailand and Bulgaria. The goal is always to ensure workers' voices are heard and trust between workers and management is increased.

### Recent activities

In 2005, we made dispute resolution, mediation skills and worker-management communication mechanisms a key focus of our programme. Training workshops were carried out for China and Vietnam (the countries where we see the greatest

incidence of labour unrest). For such sessions, we have requested the participation of government labour departments, dispute resolution lawyers, NGOs, the ILO, human resources consultancies and industry partners. Similar training was scheduled and completed in Indonesia and Thailand in 2006. An additional workshop with suppliers, government and the official state union was held in Vietnam in 2006. In El Salvador we sponsored independent training exercises for suppliers, recruitment managers and the national Ministry of Labor inspectorate. The training modules focused on workers' association rights and eliminating blacklisting practices when hiring workers who have union affiliations.

#### **Our position on child labour**

The position of the adidas Group with regard to child labour has been outlined in our 'Workplace Standards' which state that *'Business partners must not employ children who are less than 15 years old, or less than the age for completing compulsory education in the country of manufacture where such age is higher than 15.'*

The decision about the minimum age for workers has been as difficult for us as it has been for the whole industry, and one that we have considered very carefully. Before reaching our final conclusions, we visited our suppliers' factories to investigate causes, and consulted with the UN. Ultimately, we used international precedence from the UN Convention on the Rights of the Child and the International Labour Organization Conventions since they reflect most importantly, the best interests of the young people concerned.

#### **Applying international standards**

The UN Convention on the Rights of the Child (CRC) and the International Labour Organization Convention (ILO) 138 allow for work to be done from age 14 onwards, and only under certain conditions. The Social & Environmental Affairs team (SEA team) ensures that these conditions are fulfilled by suppliers who employ people under age 18. While we do not intend to promote juvenile employment we believe that supporting the conditions of these international standards is more consistent than completely banning the employment of any worker under age 18.

In most countries the labour law will not allow people under 16 to work, and between the ages of 16 and 18 there are strict limitations about the kind of jobs that can be done, and the number of hours

worked. We require our suppliers to comply with these laws and to pay people below the age of 18 at the same rates as people over 18. We do not allow our suppliers to have young people working for long hours in their factories, or on night shifts, or near heavy machinery.

#### **Monitoring age**

An important monitoring task is to check evidence of the workers' ages. Factories are required to keep copies of birth certificates, identity cards, or other legal proof of age for everyone of their employees. These monitoring findings indicate that over 99% of workers making our products are aged 18 years or older. For factories employing workers between ages 15-17, we monitor to check that all aspects of juvenile employment conditions are met.

#### **Continuing education and training**

In a small number of countries formal education finishes at age 14 and people are legally allowed to work at 15. To ensure that children below 15 do not work, we engage in Pakistan and India with programmes led by the International Labour Organization and Save the Children. These programmes are intended to improve local schools and protect family incomes when children stop working.

As part of the programme led by Save the Children, a local NGO assessed the education needs of children in Sialkot and then devised and delivered education and training interventions. The programme was partly funded by the adidas Group. To date, there are 17,768 children in 123 government schools who have directly benefited from improved school facilities and access to better education.

#### **Football stitching centres**

In 1997, the ILO, UNICEF and the Sialkot Chamber of Commerce and Industry signed a partner agreement to eliminate child labour in Pakistan's football manufacturing industry. As part of its commitment to that agreement, the ILO established an independent workplace monitoring system to check for underage workers in registered stitching centres. adidas has three football suppliers with registered stitching centres in Sialkot.

During the peak production period for the 2006 FIFA World Cup™ we commissioned an independent review to develop a more rigorous monitoring system for the stitching centres. This more effective

monitoring system prevents the employment of underage workers and minimises the risk of contracting with home based stitching operations.

### Approach to health and safety

We expect our suppliers to provide a safe and hygienic working environment for all their employees. Nothing less is acceptable. To make this a reality, we will in future be making it a requirement for all our business partners to establish a health and safety management system, such as OHSAS 18001. Our aim was for all our footwear suppliers to be certified in OHSAS 18001 by the end of 2006. 100 per cent of adidas footwear suppliers producing for the international export market met the target and obtained certificates.

Major apparel and accessories and gear suppliers were certified during 2006. Our initiatives focused on preparing the SEA team and our business partners for an increased emphasis on management systems and in 2007, we will work with other key suppliers to establish effective health and safety management systems.

#### Training the SEA team

To provide the necessary support and evaluate the effectiveness of a health and safety management system, all team members have received introductory training in OHSAS 18001. Selected team members attended an in-depth OHSAS 18001 Lead Auditor course, recognised by the International Register of Certificated Auditors, UK (IRCA). The participants now know how to establish an OHSAS management system from inception through to implementation. At the end of 2006, there were four IRCA accredited auditors in the SEA team.

#### Training adidas personnel

In 2006, numerous training sessions were provided by SEA to adidas Group employees including staff from Operations, Product and Quality Management.

#### Training suppliers

Training is provided to suppliers to influence the prevailing management culture, including environments where compliance has not been prioritised and with new suppliers in the Group's supply chain including those producing for Reebok, Reebok-CCM Hockey, and Rockport. In 2006 more than 2,500 people were trained by SEA staff.

#### Helping small and medium size enterprises (SME) implement HSE management systems

At the end of 2004 we commissioned an independent consultant to develop a set of industry specific procedures and guidance to help SMEs establish and implement an occupational health and safety management (OH&S) system. For those very small suppliers with few workers and limited resources, this package will:

- Raise the awareness and importance of occupational health and safety
- Help determine the key occupational health and safety impacts and practices for SMEs
- Demonstrate the basics for developing generic guidance, procedures, and work instructions to support the development of a documented OH&S management system, in general compliance with the requirements of OHSAS 18001.

In 2005, two apparel suppliers were selected to prepare them for OHSAS 18001 certification. Both suppliers achieved certification at the end of the year. Based on the experience from these suppliers, a manual was developed with generic guidance, procedures and instructions to operate and maintain a world class OH&S management system. This manual is being distributed to other small and medium sized enterprises in the supply chain.

#### Next steps

Following the acquisition of Reebok and the merger of the adidas and Reebok compliance programmes, the Group's existing guidelines in Health, Safety and Environment will be revised in 2007 and will include specific management guidance for small and medium suppliers. The new guidelines will follow the original format of the HSE Guidelines, but with clearer and more specific supplements. To accommodate ever more complex manufacturing processes, sections will be added to reflect those actual working environments.

#### Selection of HSE certification bodies

Globally adidas Group suppliers have a wide selection of health, safety and environmental certification bodies to choose from. However, in developing countries many certification bodies are not subject to any regulatory constraints and provide little assurance of integrity and accountability. For this reason we have selected reputable international certification bodies, and suppliers are encouraged to choose from our nominated list of certifiers.

In order to fulfil our requirements, each nominated certification body must:

- operate according to OHSAS health and safety management system
- be recognised by the government authorities where they are located and operate in strict accordance with international standards
- be subjected to peer assessment by other recognised international accreditation bodies
- have been accredited by the relevant institution, such as UKAS in the United Kingdom
- be located in at least three of our major sourcing countries
- incorporate our 'Workplace Standards', employment and health and safety guidelines.

#### **Promoting occupational health initiatives**

In 2004, we collaborated with other brands to organise occupational health (OH) training at our footwear factories in Asia. International SOS, a medical provider, was invited to develop and implement the training programme, which began in China with a review of the OH conditions in the factory clinics and staff facilities and an assessment of training needs. Based on this review, a series of ten training sessions were held attended by medical doctors, the factory management responsible for health issues, and safety officers.

In 2005, the occupational health doctors' training for three sourcing countries – China, Indonesia and Vietnam – was completed. A follow-up audit found general improvements in clinical services.

In 2006, two occupational health training sessions were organised for suppliers. The training focused on identifying symptoms of toxicity and reducing chemical exposure.

#### **2006 supply chain activities**

SEA sponsored an HSE Quiz Competition, launching it with 80,000 workers in the Asia Pacific region. This competition was designed to increase health, safety and environmental awareness at all levels of the workforce. Selected suppliers organised the competitions at their facilities and contributed a factory champion to the grand final competition.

To enhance the competency and skills of safety managers in factories and to promote self-governance by our suppliers, we launched the safety officers' registration concept in 2005. The programme aims to recognise the profession, the

occupational health and safety practitioner and the committed individual who helps to improve standards of Occupational Health and Safety in the supply chain. While dependent on the factory size, the concept clearly outlines the required skill sets, roles and responsibilities of safety managers as well as their training requirements. In 2006, the concept was replicated and successfully rolled out with selected suppliers in Vietnam and Cambodia. The relevant training was conducted by local SEA staff.

In 2006, SEA participated in the CSR Forum 2006, jointly organised by China's Ministry of Commerce and the UN's Global Compact Office, to share experiences in implementing HSE programmes with the Group's supply chain.

### **Supporting guidelines**

The 'Workplace Standards' are a set of rules that our suppliers must abide by, but to illustrate how suppliers should implement our standards, we have created a set of guidelines for use in factory settings. These expand on our 'Workplace Standards', giving detailed instructions and practical examples for implementation.

The guidelines are also used by our SEA team to:

- determine whether a supplier is complying with our standards
- advise and train our suppliers in improving their performance.

We regularly create new guidelines and revise existing ones. There are currently six guidelines and those six are further complemented by specific supplementary materials. The six guidelines are:

- Guidelines on Health, Safety and Environment
- Guidelines on Employment Standards
- Guidelines to Best Environmental Practice
- Worker Cooperative Guidelines
- Enforcement Guidelines
- Guidelines on Sustainable Compliance

In the course of 2006 the major components of our guidelines were reviewed and revised.

#### **Guidelines on Health, Safety and Environment**

The HSE Guidelines are the result of the numerous HSE audits conducted with external specialists since the inception of the SEA programme. The guidelines contain comprehensive written instructions, photographs, charts, symbols, and specific

examples of good and bad HSE practices. Several language versions are available to suppliers. These guidelines are also complemented by specific supplementary guidance materials.

#### **Guidelines on Employment Standards**

The guidelines set out the employment standards, case studies and examples of common non-compliance, suggested systems and solutions for avoiding non-compliance, documentation requirements, and relevant international laws. Several language versions are available to suppliers. These guidelines are also complemented by specific supplementary guidance materials.

#### **Guide to Best Environmental Practice**

Designed as the third component in managing social and environmental affairs, this guide aims to help our suppliers meet the environmental requirements of our 'Workplace Standards' and move beyond regulatory compliance. The guidance illustrates how to follow sustainable business practices and reduce costs by using energy efficiently, reducing waste and preventing pollution.

#### **Worker Cooperative Guidelines**

Our fair wage study uncovered the clear value of workers' cooperatives so we commissioned two labour NGOs to research and write guidelines on establishing a workers' cooperative. The guidelines cover key criteria for success and how to avoid common pitfalls.

#### **Enforcement Guidelines**

First finalised in 2004, then revised again in 2006, the Enforcement Guidelines cover the principles of enforcement of the 'Workplace Standards' and the range of remedies for breach of standard. Such sanctions or remedies include reducing orders, commissioning third-party investigations, and as a last resort, terminating the manufacturing agreement.

#### **Guidelines on Sustainable Compliance**

As stated in the 'Workplace Standards', we expect our suppliers to deliver continuous compliance improvements in their operations. This means that business partners must internalise compliance and take ownership of their activities that ensure long-term, consistent compliance execution. To internalise the Standards means developing effective systems to manage employment and HSE issues. To maintain these systems management must be engaged and the necessary resources

committed.

The Sustainable Compliance Guidelines were designed to be a reference point for suppliers establishing an internal compliance programme. They were developed in 2004 and introduced to strategic suppliers in mid 2005. The Guidelines defined specific measurements, spread over timelines up to three years that would inform the SEA Key Performance Indicator. In 2006, the Guidelines were used to help define the SEA KPI components of the Group's Sourcing initiative, the Global Apparel Strategic Alliance (GASA) world class supply chain programme.

During SEA's 2006 integration activities, it was decided that the distribution of these Guidelines be restricted to a small group of strategic suppliers. To the newly emerging and complex supply chain, most of them small and medium sized manufacturing sites, many of the Sustainable Compliance Guidelines were beyond their financial or professional means. A simpler and more direct connection to the factory's KPI was needed so the strategic compliance planning used with Group licensees was customised and launched with SMEs. The strategic compliance plan was developed as an executive level, 3-5 year, detailed investment and activity plan for the KPI's six units of measure. It is intended to have a direct linkage with the SEA KPI and to track a supplier's performance over time. During 2006, approximately a dozen suppliers started or implemented strategic compliance planning. In 2007, the goal is to see 150 suppliers develop strategic compliance plans.

### **Our supply chain**

We work with more than 1.080 independent suppliers from around the world who manufacture our products in 65 countries. Many of these are in one of the following six countries: China, India, Indonesia, Thailand, Turkey or Vietnam.

Our supply chain is global and multi-layered, with many different types of business partner some of whom are directly contracted, others who are not. Our influence in terms of social compliance is linked to the strength of our partnerships, and is often proportional to scale and stability of the orders placed with our suppliers. For this reason we aim to further consolidate our supply chain, with fewer

larger factories, with higher order volumes.

**Types of supplier**

Suppliers fall into five broad categories:

- Main suppliers
- Subcontractors
- Material and other service providers
- Licensees
- Agents

**Main suppliers**

Suppliers that have a direct contractual relationship with the adidas Group for the supply of products, whether for export or domestic market consumption. We call these Tier 1 suppliers. The largest of these have multiple factories and manufacturing sites across several countries.

**Subcontractors**

These are factories that have been subcontracted by our suppliers. They have no direct contractual relationship with the adidas Group, however, we do require them to be compliant with our 'Workplace Standards' before authorising them as subcontractors.

**Material and other service providers**

These suppliers may not have a direct business relationship with the adidas Group, but supply goods and services to our main suppliers. We call these Tier 2 suppliers. Within this category, there are nominated material suppliers with whom we work.

**Licensees**

Independent companies which manage the design, production and distribution of specific products, under license to the adidas Group.

**Agents**

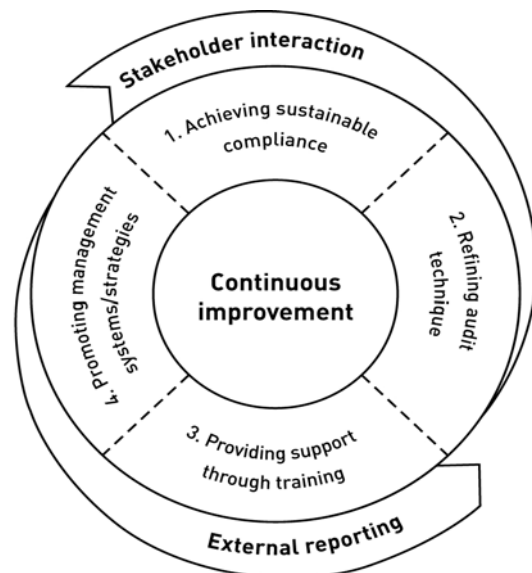
Independent companies that determine where products are manufactured, manage the manufacturing processes, and sell finished products to the Group.

Reebok has historically placed a significant number of apparel orders through agents and licensees, increasing the need to address effective compliance in an indirect sourcing model. The Group's Global Sourcing team has decided to consolidate orders with the best-performing core suppliers. So during 2007 and 2008 there will be a phased reduction in the number of agents used.

**Managing our suppliers**

We have created an SEA management cycle to describe the way we manage compliance performance by our suppliers. It has four elements:

1. Achieving sustainable compliance
2. Refining our audit technique
3. Providing training support
4. Promoting management systems for Human Resources and HSE



**1. Achieving sustainable compliance**

Our strategy is based on a long-term vision of self-governance in our supply chain where suppliers take ownership of their compliance programme. To achieve this, we need to act both as inspectors and advisors – assessing management commitment to compliance and the effectiveness of the programme, and providing help and support to suppliers to ensure success in the long term.

**2. Refining our audit technique**

Effective compliance needs committed management that is responsive to feedback and our factory rating system needs to be able to measure this. By refining our auditing approach, we will be more able to close the compliance gap where suppliers are delivering practices in a superficial, opaque, and ineffective way.

### **3. Providing training support**

We are committed to facilitating supplier compliance with our 'Workplace Standards'. We therefore offer training on all key issues including labour, H&S and environment – either led by SEA or a qualified external service provider. This training can be customised for a single supplier, or be provided to a number of suppliers in large group sessions. We also provide training with other brands that source from the same factory.

### **4. Promoting management systems for Human Resources and HSE**

We promote effective human resources, health & safety and environmental management systems as an effective way to internalise continuous improvement, and we have now made implementing an environmental management system mandatory for all our core suppliers. Strategy development and execution must be in the hands of qualified, committed and capable middle managers who are supported and empowered by senior management. The Lean manufacturing initiative and SEA activities strive to be collaborative and ensure that suppliers establish systems that support fair, healthy and safe work conditions, and deliver improved efficiency and productivity.

### **Tackling root causes of non-compliance**

To drive effective solutions you need to know the root cause of problems. In 2005, we defined a root cause of the problems suppliers had implementing effective management systems. The employment of untrained HR and HSE managers was widespread in the supply chain. Little was done to retain those who had been trained to proficiency and so there was a very high turnover of personnel in these positions. A team that is constantly changing cannot perform.

As a result, SEA reduced the focus on training managers and started to promote the registration of qualified management system professionals. We collaborated with other brands to establish a qualified marketplace of candidates. Additional training and guidelines on occupational health were developed for the factories' medical staff.

## **Monitoring compliance**

We audit our suppliers to ensure they are complying with our standards. Independent monitoring of our suppliers has also been carried out for the past six years.

### **A new approach to monitoring**

In 2004, we introduced a new approach to monitoring our suppliers, which we call 'strategic monitoring'. Previously suppliers 'waited' for audits by SEA field staff that identified non-compliances before taking any remedial action. This reactive compliance model proved ineffective leading to incremental or sometimes purely cosmetic changes in performance rather than sustainable compliance.

### **How strategic monitoring is different**

Strategic monitoring rigorously assesses compliance risks and identifies the root causes of non-compliance. Auditors do more preparatory work and then check performance against a risk list customised for each factory that is monitored. As well as monitoring compliance performance the new system evaluates the effectiveness of compliance systems and the work of their administrators. This in turn leads to a more precise evaluation of training needs and encourages suppliers to implement HSE and HR management systems.

### **Fewer factories visited more often**

This approach means deeper monitoring of fewer suppliers, where factories may be visited two or three times more often than before.

For audit numbers, see our performance data section on our website.

### **Pre-approval of new suppliers**

All potential new suppliers undergo an assessment carried out by the SEA team, and orders cannot be placed with a new supplier without SEA approval. By setting a high entry bar for potential and new suppliers we avoid getting into business relationships with suppliers that have serious workplace issues and little means of improving unacceptable conditions.

### **Developing strategic compliance in 2006**

Strategic monitoring and its risk-based approach were further expanded in 2005 by updating and revising the SEA audit tools and KPI. Training in the practices of root cause identification, interviewing techniques, and change management was introduced. A new form of the action plan for remediation was developed along with institutional history and diagnostic tools.

With the acquisition of Reebok in early 2006, the development of a strategic monitoring methodology

was quickly re-aligned to include the sustainability audit development work done by Reebok Human Rights programme staff. This assimilation immediately expedited the development process. Multiple existing audit tools used in both programmes were culled down to two models, the Initial Assessment (for new suppliers) and the Sustainability Assessment (used for all factory visits after the first). The SEA team has been using the Initial Assessment format since mid 2006, and development continues for the Sustainability Assessment, to be rolled out in late 2007.

Both methodologies have been successfully linked to the new KPI factory rating, and the strategic compliance planning process. The latest version of the KPI, which measures the delivery and effectiveness in six compliance units of measure, has been in full use during 2006. Strategic compliance planning, originally developed to manage adidas brand licensees' compliance activities, was expanded to use by suppliers. While neither tool replaces the monitoring process, they have been designed as management benchmarks to track overall factory compliance performance and to inform decisions for investment and relevant activities.

We are planning to extend our strategic compliance approach to all of our licensees and agents from 2007 onwards.

### Verifying compliance

Both Reebok and adidas have played a pivotal role in the formation of the Fair Labor Association (FLA), a tripartite organisation of companies, universities and NGOs dedicated to the sustainable improvement of workplace conditions. Through the FLA, we seek to provide verified information about our programme to stakeholders. As a participant of the FLA, the adidas Group commits to the labour standards in the FLA code of conduct, extensive internal monitoring, external monitoring by independent monitors, to remediate and prevent instances of non-compliance, public reporting, and to participate in the FLA's third-party complaint system.

In 2004 and 2005, the Fair Labor Association (FLA) accredited the individual compliance programmes of adidas and Reebok. This indicated that we satisfactorily completed an initial three-year

implementation period. The FLA found that both brands were in 'substantial compliance with FLA requirements to implement a rigorous workplace code of conduct in factories making the company's products'. In 2006, both brands remained individual participating companies of the FLA but under a single operational management. In 2007, the adidas Group, including the adidas and Reebok brands, will assume the role of an FLA participating company. This means the FLA will evaluate the SEA programme as an integrated entity operating under a single management team, with a single but enhanced set of policies and practice. The next FLA evaluation and programme re-accreditation is scheduled for 2008.

For the past five years FLA-accredited independent monitors have conducted monitoring visits to suppliers of the adidas Group. In 2006, external FLA-accredited independent monitors conducted:

- 35 monitoring audits
- 8 independent external verification visits

### Capacity building and outreach

Capacity building and outreach during 2006 included developing training needs assessment, supplier strategic planning, industry collaborations, and a more defined approach to Freedom of Association and worker management communications. Service providers were identified in the regions, and brand collaboration strengthened through joint projects. We have worked on:

- Training
- NGO outreach
- Government outreach

#### Training

There was active participation by SEA in the FLA's Central America Project that delivered training on best practice guidelines for hiring, dismissals, grievance and discipline to Central American labour inspectorates, maquila associations and suppliers. SEA attended Freedom of Association training at the Cornell University School of International Labor Relations. These measures contributed to the subsequent refinement of the new KPI's component for freedom of association (FOA) and the evaluation of suppliers' respect for worker representation and dispute resolution.

### **Training in Asia**

Staff in China, Thailand and Vietnam participated in FLA-run training for workers on Guideline of Good Practice on Hiring, Termination, Discipline and Grievances, while staff in Vietnam attended NGO training on managing HIV/AIDS in the workplace. SEA have supported internal business continuity planning in Asia, and training for operational staff in Vietnam, on preventative measures related to Bird Flu.

During 2005 and 2006, SEA Asia strengthened internal HSE capacity by attending related training for OHSAS 18000 Management System lead auditor certification and BSI (British Standards Institute) Fire Safety Engineer certification.

As part of adidas strategic initiative to improve factory and production efficiencies, SEA continued to participate in LEAN training, ensuring the synergies between the HSE programme and LEAN concepts.

In 2006, SEA attended training sessions designed to prepare staff to train the trainers (TOT). External training experts were commissioned for this work.

SEA staff in China continued to participate in the Human Resource Management System (HRMS) pilot, collaborating with other brands and the NGO TUV Rheinland. 2006 activities included training on China labour law, the recruitment and selection of workers and defining obligatory compensation and benefit award practices.

To build capacity and to support the ongoing rollout of HRMS in Asia Pacific factories, selected SEA staff in Indonesia, Vietnam and Thailand attended Human Resource training in Indonesia and Singapore.

### **NGO outreach**

In the Americas, there was continued outreach with NGOs and workers in El Salvador and Honduras, including worker consultations to verify SEA's process for assessing compliance risks. There were SEA training sessions on strategic compliance planning for selected key regional suppliers and the Maquila Industry Associations in Honduras and Guatemala were engaged frequently to clarify compliance expectations, local laws, and sustainable compliance activities. In Europe there were continued SEA training sessions on strategic compliance planning for various key regional suppliers. In China and Vietnam SEA worked closely with local arbitration bodies, external consultants

and the ILO, to develop and run dispute resolution training for suppliers.

Efforts to strengthen occupational health continued, with training for suppliers on OHSAS 18000 management systems in China and medical training for the clinicians in key apparel suppliers in China, Indonesia, Thailand and Vietnam. Service providers were identified in Indonesia for customised Human Resource (HR) training and selected key suppliers participated with brands in a HR management systems workshop hosted in China, with the objective of developing tailored training modules for the industry.

In 2006, SEA supported the execution of a medical coverage programme with a local service provider for redundant workers at three closed footwear factories in Indonesia.

SEA Vietnam continues the engagement with Marie Stopes International and the reproductive health and HIV/AIDS project. In 2006 there was a focus on training the trainers (TOT), static and mobile clinics for factory workers and the community, and SmartWorks TOT for the HIV/Aids awareness project in factories.

During 2005 and 2006, and in collaboration with several safety and health service providers, SEA conducted HSE training for suppliers. Topics included occupational health and safety management systems, and systems to ensure good hygiene in food handling. Pakistan based SEA staff worked with a local supplier and the NGO Disha to identify employment opportunities for workers with disabilities.

In Cambodia, there is an ongoing relationship with the ILO and the Better Factory Programme, in terms of monitoring and building relationships with local government and other brands. In China, the SEA team continues to work with an Educational Development Centre project addressing migrant workers issues.

In Vietnam, Thailand and China, the SEA team engaged with the ILO, the American Center for International Labor Solidarity, and the Thai Centre for Labour Rights to build supplier awareness of Employee Welfare Committees and Collective Bargaining Agreements.

### Government outreach

Government outreach in Central America focused on promoting training opportunities for labour inspectorates and the resolution of compensation for workers of the Hermosa apparel factory in El Salvador that closed in May 2005.

Following the factory closure, the SEA team began an investigation with the local NGO Grupo Monitorio Independiente El Salvador and the compliance representative of the adidas main supplier who subcontracted with Hermosa. In December 2005, following the 3rd party complaint to the FLA, an expanded investigation team was formed including representatives from other brands.

From November 2005 until February 2006, almost three dozen engagements with stakeholders were held. This included the Minister and senior officials of the Ministry of Labour, the Ministry of Economy, the US Embassy, local NGOs and a senior prelate of the Catholic Church, the trade union confederation Fenastras and their affiliate STITTAS, the trade union FEASIES, approximately 65 Hermosa workers, the Hermosa factory owner and his legal counsel, the Labour Tribunal, officials of ISSS (Institute of Social Security), and local banks.

The Ministry of Labour later committed to hiring 69 new labour inspectors, effectively doubling the labour inspectorate.

We continue to have discussions with the US Embassy and US State Department about government consultations with El Salvador in light of CAFTA provisions for effective management and regulation of labour laws. In particular, we will continue to engage the national government requesting protection of all workers rights to compensation as guaranteed under the national constitution.

See the Statements section on our website for more information on Hermosa.

### Government outreach in Asia

In 2006, Asia Pacific outreach with government agencies continued. Collaborations with Indonesia's Manpower Department and other brands included training for suppliers on employment contracts and settling industrial disputes. The Ministry of Labour and Industrial and Trade Ministry were engaged to discuss effective management of factory closures.

In Vietnam, the Ministry of Labour and Invalid Social Affairs and the Vietnamese General Confederation of Labour were engaged for regular briefings on the ever more important issue of strikes at Foreign Direct Invested Enterprises.

The Thailand Labour Ministry was engaged for clarification on legal interpretations for the wage components, including piece rates systems and incentives earned during overtime. In Cambodia there was a collaborative effort with BSR, the ILO, Better Factory Cambodia and other brands to engage the government in efforts to safeguard union leaders in the country after the killing of two union leaders in 2004 and 2005.

In China, SEA participated in seminars with the Guangzhou Labour Department regarding the social insurance system, labour law updates and managing industrial relations. The Guangdong Labour and Social Security Department also met with SEA frequently to review workplace injury policies and practice.

## Enforcing compliance

### Enforcement guidelines

In 2005, we issued the enforcement guidelines to our suppliers. The guidelines cover the principles of enforcement of the 'Workplace Standards', and those sanctions or remedies we will apply where the Standards are breached. Such sanctions or remedies include:

- termination of the manufacturing agreement – in situations of severe or repeat non-compliance
- stop-work notices – in life-threatening situations or where the manufacturing process is likely to have significant negative consequences for the environment
- third-party investigations – where persistent or repeat violations of the 'Workplace Standards' or local laws have become a matter of public interest
- warning letters – in cases of ongoing and serious non-compliance
- reviewing orders
- commissioning of special projects – to remedy particular compliance problems.

### Two types of non-compliances

In 2006 and during the integration of programmatic policies and practices, the breaches of the

'Workplace Standards' were categorised into zero tolerance points and threshold issues. Zero tolerance includes prison labour, serious, life threatening health and safety conditions and repetitive or systematic abuse. The Enforcement Guidelines for zero tolerance is the supplier's disqualification from the adidas Group supply chain. Threshold compliance issues include serious employment issues, serious health, safety or environmental issues and any combination of the two. The Enforcement Guidelines for threshold issues can disqualify a new supplier from production or lead to enforcement actions with existing suppliers.

#### **Next steps**

The challenge in 2007 is to expand the Enforcement Guidelines to engage third party representatives in indirect sourcing models. Existing Group relationships will have to be modelled to define clear and effective lines of responsibility with the third party supply chain and the adidas Group.

#### **Warning letter system**

We strongly believe in a partnership approach, and where a supplier is performing poorly in terms of 'Workplace Standards' compliance we will work closely with them to find solutions. However, where we find ongoing and serious non-compliances and a lack of commitment on the part of management to address the issues, we will, when appropriate, issue a formal warning letter.

For threshold compliance issues, three warning letters will usually result in an immediate recommendation to terminate. In very serious cases or in cases of zero tolerance non compliance, a single letter will be issued advising our suppliers that SEA has recommended the business relationship be terminated. Our Sourcing, Business Unit and Legal departments would then follow-up with a formal notification of the end of the business relationship.

### **Rating our suppliers**

The new 'Workplace Standards' KPI was completed in 2006, and widely applied with the global supply chain. Mainstreaming of the KPI, started in Q4 of 2005 with desktop exercises for supplier applications, continued in 2006 with rating exercises integrated into the majority of field monitoring activities. Newly integrated supply chains for

Reebok received KPI rating exercises. Plans were begun to address KPI application in indirect sourcing models, and adidas International Sourcing incorporated the SEA KPI to the overall supplier KPI rating.

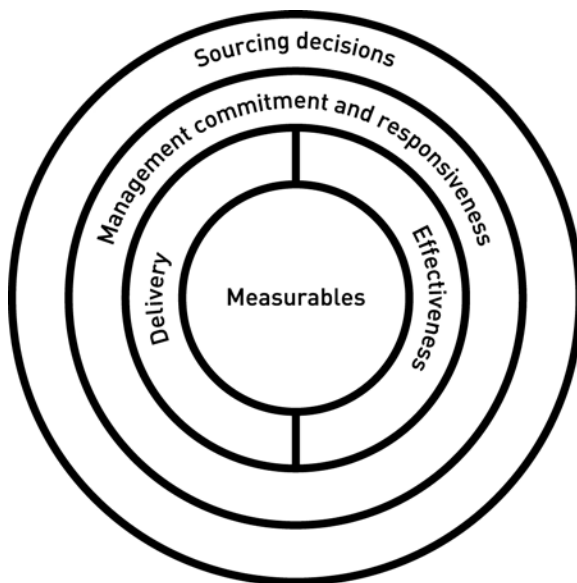
#### **The KPI's six units of measure**

1. Measuring management commitment and responsiveness to a strategic compliance plan. The planning document defines each unit of measure from the supplier KPI so there is a direct linkage between 12-month compliance activities and opportunities for improvement identified during SEA monitoring. Additionally, the plan spells out details for employee retention, compliance-related investment, relationships with third parties and local government, crisis management, and project development on critical compliance issues.
2. Measuring supplier management systems for HR and HSE includes an evaluation of certifications for environment and health & safety, development of HR and HSE systems, retention of qualified professionals for those management systems, and internal audit assessments of labour and HSE.
3. Measuring management worker communications and industrial relations focuses on the factory's ability to resolve disputes, respect forms of worker representation, develop effective grievance procedures and promote sustainable worker-management communications. There is an evaluation of the communication committee's effectiveness and sustainability, and the training needs assessment used by the factory to develop worker and management training.
4. Measuring the delivery and effectiveness of internal training for factory staff focuses on the process for a training needs assessment, the scheduling and execution of the training programme, and the budget allocated for training. Trainers are evaluated for their skill, knowledge and experience. Factory records for training and the protocols for reporting these activities are also reviewed.
5. Measuring transparency in communication and reporting focuses on proactive factory reporting of self-assessment audits and action plan progress. There are additional benchmarks for determining if workers are coached, verification of document authenticity and communication of the 'Workplace Standards' to the workforce and subcontractors.

6. Measurements for compliance activities that focus on the factory's management response to findings of non-compliance, remediation, or enforcement actions.

In 2007 the application of the SEA Key Performance Indicator will be further extended to the Reebok brands and licensee, agency and distributor supply chains. More Tier 2 suppliers (such as embellishers) will be monitored and evaluated for KPI ratings.

**Our factory rating system diagram**



**Case studies**

We include here three case studies that illustrate how we are working with suppliers to improve their compliance performance. These suppliers are all involved in manufacturing football products:

- Increasing management commitment at Sports Gear, Vietnam
- Independent review of compliance practices in football production, Pakistan
- Health and safety improvements at Trikotek Tekstil knitwear factory, Turkey

**Increasing management commitment at Sports Gear, Vietnam**

Vietnam is a key sourcing country for the adidas Group, with 17 footwear, apparel and accessories and gear factories making various products for a number of different markets. Like many other countries in South-east Asia, the local worker

population is managed mostly by Taiwanese, Korean, Malaysian and Singaporean manufacturers. In step with Vietnam's development, our suppliers are going through a period of rapid growth. In recent years, a new wave of migrant workers has moved from north and central Vietnam to the south where our suppliers' factories are located. This creates a demanding set of communication and industrial relations issues that need to be managed very carefully.

**Healthy competition**

To help our suppliers in Vietnam handle the rapid changes, the SEA team has introduced a system of peer reviews. Elsewhere in the region, the SEA team has led several years of regular workshops, discussions groups and on-site training for factory compliance coordinators. In Vietnam, we've taken this to the next level. Peer reviews and the subsequent healthy competition between suppliers are starting to drive management commitment rather than top down pressure from buyers' compliance teams. Each factory 'competes' to host, design, and manage workshops, cross-auditing exercises and training programmes. Our staff act as observers and provide technical support where necessary.

**Increased commitment**

This form of constructive peer pressure has contributed to a significant improvement in the attitudes and management commitment to the SEA programme at Sports Gear. The change is particularly encouraging because Sports Gear has one of the most sophisticated facilities in Vietnam, manufactures footwear products for FIFA World Cup™ but was not a top compliance performer. The factory has hired a full-time compliance professional to manage ongoing labour and HSE issues on the factory. At the same time, reluctance to participate in compliance initiatives has been replaced by a growing awareness that not only should the factory participate in such projects, but that it should be an industry leader in Vietnam. Management has fully supported:

- the SOS occupational health training project [see Suppliers and workers – approach on health & safety]
- the MSI reproductive health and HIV/AIDS initiative [see Community Affairs case study]
- a worker satisfaction survey and communications needs assessment

- SEA training to pilot the new strategic monitoring process [see Suppliers and workers – monitoring compliance].

Given the increasing levels of industrial disputes and other labour actions by workers in Vietnam, Sports Gear management has repositioned itself over a relatively short period and is now better able to manage and protect its 8,700 (and growing) strong workforce.

#### **Independent review of compliance practices in football production, Pakistan**

For the past 70 years, Pakistan has been a major supplier of hand-stitched footballs. The town of Sialkot, in the Punjab region, is the main centre for production. The presence of child labour came to light in the mid 1990s and was addressed through an industry-wide initiative supported by the ILO and UNICEF. As a result, an independent child labour monitoring body which is now self-governing, was established in 1997. The underlying issues of poverty, employment and access to schooling were addressed through a combination of educational and social development programmes. See Sudhaar case study in the Community affairs section.

#### **About the stitching centres**

adidas places orders for hand-stitched footballs with three main suppliers who produce the ball components and inspect, pack, and ship the balls. The stitching of the balls is contracted to dedicated stitching centres in the rural community surrounding Sialkot. adidas has sourced footballs from this region for 32 years.

The stitching centres workforces vary in size from 20 to 450 workers. The larger centres are generally located close to or within the grounds of the main suppliers. These suppliers normally operate a total of 70 stitching centres but due to the volume of orders for FIFA World Cup™ products the number of stitching locations increased to a peak of 121 in October 2005. Of these, 18 are women-only stitching centres.

#### **Reviewing and improving performance**

A significant challenge for us in 2005 has been maintaining the integrity and security of the supply chain through the FIFA World Cup™ peak production period. We commissioned an independent review of the monitoring programme after SEA monitoring visits in 2004. We identified the need to improve the payment of social benefits to stitchers in regular

employment, and to strengthen monitoring practices and stitching centre coverage during the anticipated peak production periods.

The review highlighted the weaknesses of the current compliance monitoring, with insufficient coordination and cross-checking. A new monitoring model was developed using the combined resources of all three factories monitoring staff, and random verification by adidas SEA and an independent third party. Monitoring activities for checking infrastructure, safety, stock registers, attendance records, wage payments and proof of age were all significantly improved.

The review resulted in an increased frequency of monitoring visits, improved timeliness of reporting, and the identification and resolution of product tracking and labour issues. Some of the substandard stitching centres were closed.

#### **Health and safety improvements at Trikotek Tekstil knitwear factory, Turkey**

The adidas Group has buying relationships with 17 main suppliers in Turkey. adidas has been buying football team scarves from Trikotek Tekstil, a company with 140 workers located in Istanbul since 2003.

As with other Turkish factories, there were a number of health and safety (H&S) non-compliances, including poor H&S management systems, the absence of an H&S policy or coordinator, insufficient emergency preparedness, no fire evacuation drills, and poor knowledge of personal protective equipment (PPE) and chemical handling.

#### **Advising as well as auditing**

Our audit process not only identifies the root cause of each non-compliance but also incorporates the SEA Health and Safety Guidelines to illustrate the benefits and methods of remediating specific issues. For example, the factory management was not only told to conduct fire evacuation drills, but why and how to do so efficiently. Together with Trikotek's management, SEA developed a detailed action plan that was monitored regularly.

Three months after the initial audit in 2003, a second audit was conducted at Trikotek that revealed some improvements in the factory's H&S conditions. The verification included documentation of their remediation efforts. These promising results

emphasised that an effective H&S policy and a coordinator with clear responsibilities and authority were crucial for sustainable improvements.

**Taking responsibility**

Trikotek continued to improve their H&S performance. The new H&S policy and a competent coordinator helped to resolve many other H&S issues quickly and sustainably. Encouraged by the consistency of the improvements, Trikotek applied for OHSAS 18001 in February 2004, and received certification in September 2004. The factory's internal audit team now conducts self-assessment audits on a monthly basis, and has developed systems for emergency preparedness and fire fighting. They have also introduced training to improve the usage of PPE, machinery guarding and chemical handling.

A December 2004 SEA audit of Trikotek revealed the increased compliance with HSE workplace standards and the effective delivery of a management system. The subsequent factory performance rating for HSE was increased from 3 stars to 4 stars.

In conclusion, the improvements at Trikotek resulted from not merely auditing, but follow-on activities for policy development, staff competency training, policy and process implementation, and verification and reporting. This holistic cycle of H&S management is now guided by the OHSAS 18001 process.

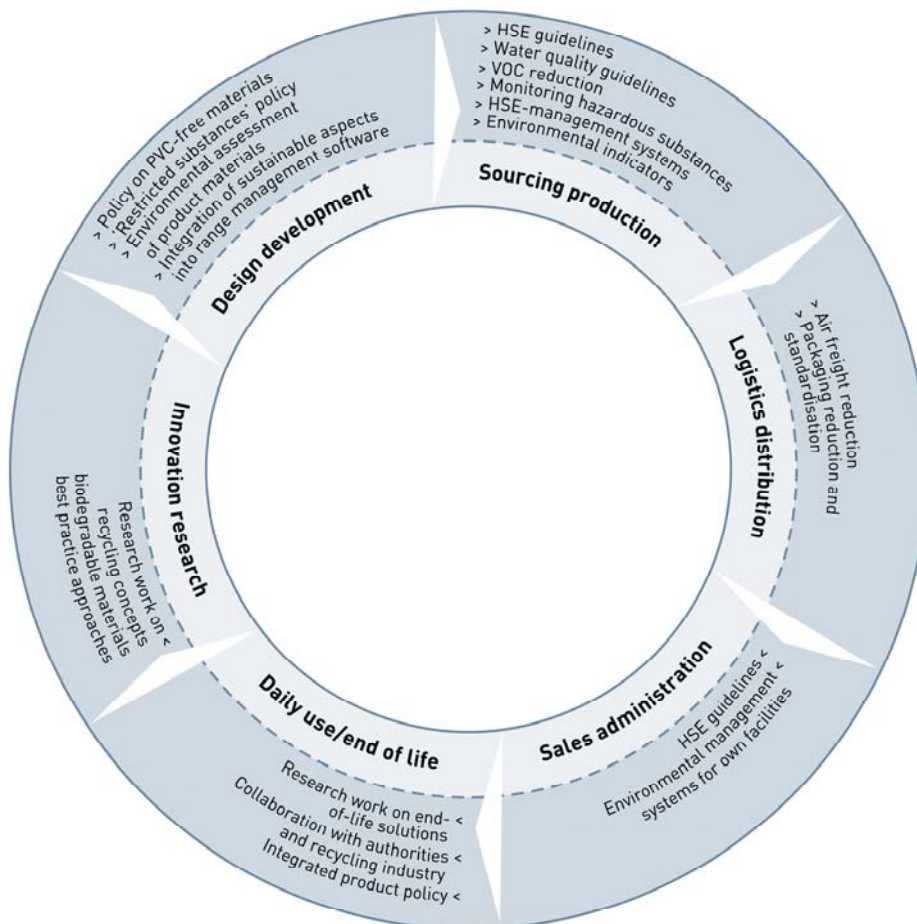
Trikotek was the first of our Turkish suppliers to successfully achieve OHSAS 18001 certification. Their example has raised the bar and we are now seeing a general improvement of HSE conditions throughout the local supply chain.

**ENVIRONMENT**

We have a responsibility to look after the natural environment both for people today and in the future. We recognise that the new adidas Group is a bigger company with a larger physical footprint, which means we have an even greater responsibility to manage our impact on the environment.

Environmental impacts occur at all stages of the lifecycle of our products, from product design to disposal. Our efforts are focused on the manufacture of our products at our suppliers' sites where more than 95% of our products are made.

We adopt a systems-based approach to managing our environmental impacts in our own production facilities and in our supply chain. Within the life cycle of our products there are two points in the product design and development process where we can make a significant difference to the company's environmental footprint. The first is in improving the materials that go into our products, and the second is in tackling pollution in factories.



## Managing environmental impacts

The best way we can influence the environmental impacts at our suppliers' factories is to encourage the introduction of environmental management systems, and we have now made implementing an EMS mandatory for all our core suppliers. Achieving certification to a management system requires factory managers to plan, manage and review their own environmental performance. This encourages them to approach the issue with rigour and the appropriate resources. Environmental management systems commit the supplier to continuous improvement.

We have harmonised the way we capture and report on resource consumption at our own factories and major sites, and have introduced similar environmental metrics for our suppliers' footwear factories. These initiatives will allow us to identify and share best practice across the whole Group – both at our own sites and in our supply chain.

### adidas Group production sites

With the acquisition of Reebok and its brands the adidas Group now operates 13 sites around the world where manufacturing takes place. Production sites are located in Germany (1), Sweden (1), Finland (1) USA (4), Canada (4), China (1) and Japan (1). These facilities produce garments, athletic footwear, golf clubs, ice hockey sticks, helmets, and blades and do screen-printing and embroidering.

The factories comply with local laws and regulations, and have HSE programmes that are managed by designated HSE coordinators. Sites in Germany and in China have been certified in accordance with EMAS and ISO 14001. Corporate Guidelines for Health, Safety and Environment have been produced at a Group level to support facility managers and HSE coordinators.

In 2007 we began to keep a systematic record of the environmental impact of the production sites that were added to the adidas Group following the acquisition of Reebok. This will allow us to comprehensively report about our environmental performance in early 2008. For an overview of the environmental performance of these sites please go to the performance data section.

In 2006, there were no legal prosecutions reported for environmental liabilities at the Group's own sites.

Here are some examples of how we manage environmental issues at our own sites:

### Scheinfeld

This small scale athletic footwear factory produces premium football boots and made to measure shoes, but also operates a warehouse and flock transfer printing department. This was the first factory in the sporting goods industry to obtain certification according to EMAS - in 1998 - and it was re-certified under the EMAS II scheme in 2001 and 2004. In 2006, the site was audited by an environmental verifier; a complete recertification is scheduled to take place mid 2007.

### adidas-Suzhou

adidas-Suzhou, part of our subsidiary in China, produces garments for the international and local market. The factory has been certified to ISO 14001 since 2002. The production manager, plant manager, office manager and administrator are qualified internal ISO 14001 auditors.

The monthly average energy consumption rose about 16% from 2004 to 2005, due to enlarging the raw material warehouse area about 70%. A further 12% area growth as well as extended installation of air condition systems led to another increase in energy usage of 15% in 2006. An external consultant reviewed wastewater quality and noise level in July 2005, with all values meeting local standards.

### Carlsbad TMAG

Starting in 2005 our site in Carlsbad, California began implementing the so-called 6S approach (Sort, Straighten, Shine, Standardise, Safety, Sustain), which led to restructuring the office and workplace layout and an improvement in its environmental and health and safety performance. This commitment to continuous improvement was further supported during 2005/2006 by an engineering risk assessment conducted by a European based consultancy. Recommendations included using a noise dosimeter, installing air circulation systems and various ergonomic aspects.

### Administration offices

Most of our sourcing offices, sales subsidiaries, warehouses and administration sites have less environmental impact than the environmental effects of manufacturing products in factories. HSE activities are managed by designated HSE coordinators or the respective facility management.

Nonetheless, besides adhering to specific local laws, Corporate Guidelines for Health, Safety and Environment have been produced to support facility managers and HSE coordinators. These guidelines provide best practice advice for workplace ergonomics, eco-purchasing of office materials and resource savings. For example, from mid-2006 onwards, at the adidas Group Headquarters in Germany, we have introduced a new generation of office paper. The paper contains chlorine-free recycled materials but provides a high-value look as requested by our design departments. Since June 2006, 14 million sheets of this innovative matrix paper system have been purchased for the HQ facilities.

#### **Building in environmental efficiencies**

We consider environmental issues whenever we design new buildings or refurbish existing ones. For example, when our global Headquarters in Herzogenaurach was redesigned from old military barracks, specific measures were taken which included using recycled building materials, avoiding energy-intensive air conditioning and installing innovative heating and cooling systems in the employee restaurant STRIPES.

#### **adidas Group HQ in Herzogenaurach, Germany - Environmental activities**

During 2006, several new facilities and buildings started their business operations at our global Headquarters, in particular the adidas brand center, the Adi Dassler sporting grounds and the adidas World of Global IT. Major events that took place at the World of Sports facilities during the 2006 FIFA World Cup caused an unavoidable increase in natural resources and energy. For more information see the performance data section.

#### **adidas North America Headquarters in Portland, USA - Environmental activities**

Salmon Safe Certification - Salmon-Safe is an independent 501(c)3 non-profit organisation devoted to restoring agricultural and urban watersheds so that salmon can spawn and thrive. The organisation is based in Portland, Oregon. Salmon-Safe land management involves conservation practices that benefit the watershed where the farm or other site is located.

In 2006, Salmon-Safe conducted an in-depth assessment of the overall land management policies and operations at adidas in Portland that directly and indirectly affect water quality and fish

habitat. Salmon-Safe's management evaluation will be augmented by a field level assessment of the site. Both policy and field-level evaluations will be conducted using Salmon-Safe's peer reviewed Corporate & University Campus Assessment Standards to assess whether the management is consistent with best practice for avoiding harm to stream ecosystems.

Boiler Plant Study - after completing a recent engineering study of the heating plant it has been determined that two heating boilers will be replaced. The new high efficiency units will be directly controlled by the energy management system.

Wildfire Risk Reduction/Native Revegetation - We are participating in a federally funded programme with the city of Portland that has two components:

1. Reduce the low lying brush on the wooded portion of our property that will reduce the fuel for a potential wildfire during the dry summer season.
2. Eliminate the non-native vegetation that has negative effects on the native trees and shrubbery that grows wild throughout the Pacific Northwest.

#### **Reebok Headquarters in Canton, USA - Environmental activities**

This facility, operating since 1999, went through an environmental re-engineering process in 2003/2004, which also covered the linked distribution centres. Systematic upgrades for the heating, cooling and lighting equipment has resulted in an annual saving of nearly 2 Million KWh per year, which is equivalent to \$200,000 per year.

An ongoing office paper recycling programme has been established as well as certain employee volunteering programmes like a car-pool sharing database, supported by transportation awareness events and Bike to Work days. In 2006, a shuttle bus to the local public transport hub was set up.

#### **Our suppliers' sites**

Our core suppliers must implement environmental management systems. Many of our Asian footwear factories led the way in establishing these systems. And increasingly apparel and accessories and gear factories are following their lead.

In 2006, 21 footwear factories were certified according to ISO 14001 and/or OHSAS 18000.

See the table of suppliers with environmental and health and safety certifications in the performance data section.

## Improving materials

Our approach is to seek to design out polluting materials and processes and increasingly to adopt sustainable materials instead.

You can read about the various initiatives we have in place that help us achieve our goal of improving materials.

- Material selection policy
- Sustainable cotton
- Recycled materials
- Eliminating PVC
- Control and monitoring of restricted substances
- EU legislation on REACH
- Integrated Product Policy
- Product safety

### Material selection policy

We do not source raw materials from any endangered or threatened species as defined by the International Union for Conservation of Nature and Natural Resources (IUCN) in their red list. We also do not use leathers from animals that have been inhumanely treated, whether these animals are wild or farmed.

Materials supplied to the adidas Group must meet local regulations. We ask our suppliers to ensure that:

- Materials be non-toxic in use and disposal
- Using materials does not cause toxic emissions during the manufacturing process
- Products are manufactured under the best possible conditions using the best available technology.

### Sustainable cotton

We further investigated the use of certified organic cotton, which is expensive and more difficult to find. It also does not sufficiently address the biggest environmental issue with growing cotton, which is excessive water use.

Taking a more holistic approach, we are part of an initiative called 'Better Cotton' that seeks to train cotton farmers to adopt a more sustainable approach to farming. This is consistent with our

general approach to build capacity in our supply chain. Together with other brands, NGOs and environmental organisations we have initiated a five-year plan, which aims to create and implement a set of better cotton standards and practices for the mainstream cotton growing industry.

Participating companies show interest to reviewing their own sourcing arrangements, looking for examples where all links on the supply chain benefit, from farmer and spinner to garment manufacturer and retailer. Finding these win-wins and encouraging more arrangements like them is crucial to achieving the project's goals to get as many buyers behind this concept as possible and so create a critical mass demanding better cotton.

In 2006, consultations with regional organisations and local agricultural institutions started in India and Pakistan, as we set up the training and checking for the field testing phase.

A full time project manager was hired on behalf of the Steering Board to support the project's development. Extended stakeholder outreach to various interest groups took place, on the governmental and official side as well as to the NGO community.

### Recycled materials

A pilot project in Vietnam experimented with recycling waste rubber soles to make new shoes and soles. To meet quality standards, different mixes of new and recycled material were tried and feedback from the customer was considered. But even though no major quality problems occurred, this concept was not applied as a global policy for all rubber applications. Reasons for this are significant colour and design limitations in applying this technology. The approach will be continued for certain rubber designs depending on the model of shoe. New technical solutions that can be applied more widely are constantly under review by the respective operational departments.

### Eliminating PVC

In 2000, we decided to eliminate PVC from our products. Alternatives have been found and introduced for most uses. Nearly 99% of our global product range is PVC-free. However, in a few countries, alternatives are not available so some local production of athletic footwear products still uses PVC sporadically.

In 2005, we continued to engage with material scientists to understand the environmental impact of chlorine-based materials. These materials are widely used in the industry as PVC-replacements. The consultations are important so we can anticipate environmental developments at an early stage. We have started to review the materials used in footwear products to determine a potential substitution wherever technically and practically possible.

During 2006 and as a result of the integration process the Group's policy to eliminate PVC was rolled out to the new Group entities, where no such programme existed. The first complete phase-out plans were executed by the end of 2006 in several product categories. For a few product applications, full PVC substitution is not achievable due to the absence of technically viable solutions. However, we have developed a mid-term programme to overcome these challenges and to consistently execute our PVC-free policy across all product categories.

#### **Control and monitoring of restricted substances**

Restricted substances are those that cause harm or are suspected to cause harm to human health or the environment. Our policy is that suppliers must avoid using restricted substances to ensure that our products are environmentally safe. In 2006 we reviewed our standards and policies on restricted substances, the 'A-01 Requirements' to make sure they were unified and we were consistently executing them to the highest standard. The policy was rolled out and implementation started within all adidas Group entities and product divisions.

Materials supplied to the adidas Group must meet the strictest local standards globally. We ask our supplier to ensure that:

- Materials are non-toxic in use and disposal.
- Using materials does not cause toxic emissions during the manufacturing process.
- Products are manufactured under the best possible conditions using the best available technology.
- Materials meet sourcing standards of retailers, customer expectations and those recommended by consumer organisations.

We inform our material suppliers regularly about new scientific findings and developments. They must prove that materials comply with our standards by providing test reports from independent external

test institutes on a regular basis. Development and production samples are checked randomly.

Read our A-01 Requirements in the Environment section of our website.

#### **EU legislation on REACH**

We have been carefully observing draft EU legislation related to chemicals called REACH (Registration, Evaluation and Authorization of Chemicals). As a company committed to sustainable practices and meeting consumer needs, we believe that the REACH initiative is an important step towards increased transparency in the use of chemical substances and preparations that result in safer products.

Due to the uncertainty about the final structure and specific requirements from REACH, it is difficult to forecast how the legislation will affect international trade agreements, sourcing and production relationships, business administration and small and medium-sized enterprises. To better understand the future implications of REACH for our business and to express our views we closely interacted with other brands, the Foreign Trade Association and EC-governmental officials.

While the REACH legislation in its basic structure has been approved by the European Commission in 2007, important parts of the Directive, Technical Guidelines, implementation procedures and lists of respective chemicals have not yet been finalised, or have been withdrawn for a further complete review by EU officials. We will continue to carefully observe developments so we are prepared to comply.

#### **Integrated Product Policy**

Integrated Product Policy (IPP) identifies environmental impacts throughout the life cycle of products and, with stakeholder cooperation, explores solutions to these impacts that benefit both the environment and business. The strategy for IPP complements existing environmental policies.

adidas has followed the IPP approach in a pilot study of athletic footwear products supported by the Environmental Ministry of Bavaria. Working with the environmental consultancy INTECHNICA, the project covered all stages of the product's life cycle, from the extraction of natural resources, through to re-use or disposal. Involving adidas representatives from many different functions, a football boot model was selected and all relevant data regarding the

environmental impact of this product from inception to disposal was collected.

### Results

The cumulative environmental impact of the boot was calculated as well as identifying the stages of the lifecycle that cause the largest impact and how we might reduce those impacts. We were also able to quantify changes in the cumulative environmental impact if materials, components or manufacturing processes were changed. The calculation tool can therefore be used as an additional decision-making aid for material selection, design and development.

### Developments in 2006

A new football boot, which was launched in 2006, was screened against IPP principles during its development in 2005 to field-test the applicability of this innovative evaluation tool. Due to significant construction differences and distinctive performance aspects it was impossible to directly compare data from this new product and the originally selected model. However, we were able to establish a calculation process that will allow us in future to compare products with the same construction complexity and to draw conclusions about their relative environmental footprint.

Based on the findings of the studies further prototypes for performance athletic footwear were designed and developed. They consider the most environmentally-friendly but also technically viable solutions, from material selection to trials with the most innovative bonding systems. Prototypes had to meet all functional and quality test requirements. During this phase a number of issues were identified which have to be fixed before the concept is fully commercialised.

### Product safety

To ensure product quality and consumer-safe products, all materials and product samples are tested in accordance with standardised material and product testing specifications and procedures.

The "Product Safety and Environmental Services" function was expanded to further strengthen the internal infrastructure and ensure the consistent application of physical, chemical product safety and conformity standards across all brands of the adidas Group. This step was taken to roll out Group-wide product safety policies, to intensify product checks and to engage more closely with the product teams on product safety issues.

In 2006, Reebok announced 2 voluntary re-calls of products. For more information on this please see the Reebok website.

## Tackling pollution

We provide support for our suppliers with guidelines and have a long-standing initiative to reduce VOC emissions. We also seek to address the CO<sub>2</sub> emissions from transporting our goods.

- Support for suppliers
- Environmental indicators
- Reducing VOC emissions
- Waste management strategy
- CO<sub>2</sub> emissions from transport and travel

### Support for suppliers

Our approach is to help our suppliers reduce the environmental impacts in their factories through advice and support. In 2000, we issued our Health, Safety and the Environment (HSE) guidelines, which have been followed by a more specific Guide to Best Environmental Practice in 2002. Highlighting best practice both inspires and practically explains how our suppliers can improve their performance.

In 2005, we conducted specific needs assessments among our suppliers to understand their environmental priorities that differ significantly from product complexity and production processes at sites. Many reported that energy consumption was one of their main concerns. The drastic increase of oil prices has affected energy costs and the high demand in energy has resulted in power shortages in factories in China, where several of our suppliers' factories are located.

In 2006, we continued the planning and preparations for a series of supplier energy efficiency workshops, which form a core element of the Group's supply chain environmental programme. This included the development of customised training materials and technical recommendations that were developed across the different product divisions with the help of an environmental consultancy. Vietnam and South-China were chosen as the countries to kick off the series of energy workshops.

Facilitated by the SEA team and operated by the environmental consultancy, the first two workshops took place in early 2007 in these countries. 101 suppliers attended the workshops, representing a

cross section of the Group's core and strategic suppliers and factories, both across divisions as well as across brands.

The workshop which was run under the theme "Energy Efficiency - Advantage for Environment and Industry" stressed the significant economic potential for industry and business and the tangible benefits to the environment. In-depth training was given on various aspects of energy management and contained a wide range of improvement suggestions for factory managers and their facilities. Another important topic was how to stay competitive and safeguard production performance while at the same time reduce pollution and its impact on global warming. Feedback surveys and questionnaires will help to further tailor and streamline our future activities for the needs of our suppliers.

#### **Environmental indicators**

A detailed set of indicators has been developed, and established mainly in our suppliers' footwear factories to measure, track and analyse the environmental footwear operations. Differences in the technical complexity of the various product models in production will always cause deviations in the data collection and interpretations.

The process of data completeness and accuracy, however, matured to a level, that enabled us to calculate the average consumption of key resources per pair of sport shoes produced by our key footwear suppliers in Asia, covering more than 95% of adidas footwear production.

Following the integration process in 2006 those footwear factories that have manufactured for the Reebok brand started to report their consumption. However the below mentioned data still only reflects the brand adidas footwear factories, as the quality of data provided by Reebok suppliers is still under review.

#### **Performance of adidas shoes**

- Energy use is 2.36 kWh/pair.
- The amount of waste water per pair is 0.045m<sup>3</sup>.
- Waste ratio in product in per cent: 7.81% of the raw leather and 11.22% of the synthetic upper material. (These figures are calculated at a stage in the process before the waste material is fed into a waste management programme.)
- Average VOC consumption per pair is 19.3g.

The indicator system is now a reliable management tool for our footwear suppliers helping them to not only measure resource consumption but also identify potential savings and set reduction targets. We will continue to assist them in maintaining these tools so they can realise these potential savings.

#### **Reducing VOC emissions**

Since 2000, we have been committed to reducing emissions of VOCs in footwear factories in Asia. Our target is average VOC emissions of 20 grams/pair of shoes. VOCs – volatile organic compounds – are found in solvents used in the manufacturing process. They can cause breathing difficulties and other health complaints.

Our footwear suppliers have reduced VOC emissions from 140 grams/pair in 2000 to 19.3 grams/pair in 2006, which includes nearly all new adidas Group footwear factories, and reflects the technical synergies of sharing information, data and sources on production questions such as water based cement systems.

We regularly measure actual exposure in the workplace by asking workers to wear monitors during their working day. Emissions measured are far below the threshold limit value. These results suggest workers are not being exposed to dangerous levels of VOCs but nonetheless we remain committed to further reductions.

See the Performance data section for more figures on VOC reduction.

#### **Waste management strategy**

Several in-depth studies and surveys have taken place, mostly with our footwear factories. An external consultant conducted investigations with our footwear partners in China, Indonesia and Vietnam. Considering the different waste amount and sources, but also the specific local circumstances, the outcome showed that it is necessary to:

- further enhance the system to measure the waste volumes
- develop more in-house recycling systems
- consider local conditions and barriers when developing new waste management approaches.

The study also recommended pooling waste material from various factories to create greater volumes and to develop organisations that could

provide a vertically integrated service from collection and sorting to recycling.

One example of how the adidas Group has been looking into ways to reduce and finally eliminate the practice of using waste for landfills is described in the case study below.

#### **Case Study: Waste Co-processing in Vietnam**

With the rapid industrialisation and population growth in Vietnam, each year the country produces more than 15 million tonnes of waste. The lack of controlling and monitoring systems, of waste treatment technology and capital resources make the need for effective waste management solutions more important than ever.

One of the country's most popular waste disposal methods is incineration. However, handling the daily waste is becoming more and more of a problem as the technology of incineration plants is very basic and therefore insufficient. In spite of these plants being assessed by the government for technical standards and gas emissions, Vietnam still lacks the technology to analyse dioxin and other pollutant concentrations. Waste collectors are not sufficiently monitored or tracked, and their backyard facilities have adopted insufficient waste treatment methods. This poses a serious threat to people and the environment as ground and surface water is often contaminated from this untreated waste. Consequently, efficient waste management is one of the biggest social and environmental challenges. One proven alternative and possible solution on the way to a "zero waste society" in Vietnam is the so called "Co-processing" technology with the help of which waste is converted into cement.

In November 2005, the SEA team invited all the adidas footwear factories to visit the HOLCIM Co-processing plant in Rach Gia, a province in the south of the country, to introduce this technology to them. The co-processing technology uses waste materials as raw material for other industrial processes, to recover energy and lower the quantities of other natural resources used. Co-processing means that waste is collected in a monitored way, packed and shipped to the HOLCIM plant where it is shredded and then melted down in special kilns. The plant uses high-tech equipment, and waste co-processing takes place in a strictly controlled environment. The factories now know what happens to their non-recyclable wastes from footwear manufacturing,

and materials can be traced throughout the production cycle.

The process of using the waste in this cement kilns is seen as very environmental sound, because:

- there is no further ash, all material remain inert in the clinker
- the high temperature process
- it is a self cleaning process, oxidising in alkaline environment
- there is a full set of state of the art monitoring and process control equipment
- it allows for full traceability of the waste flow, which is not available from local waste collectors and service providers.

In 2006, 622.3 tonnes (more than 34% of the entire volume) of the participating factories' waste was used for co-processing, and so will be diverted from low level incinerators or landfill, the most common waste management methods in Vietnam.

For 2007, greater quantities (50%) are targeted to become part of the programme, as well as the extension of the co-operation to more adidas Group suppliers located in the area. For the adidas Group in Vietnam, this is a great opportunity to set an industry benchmark for waste management in our industry, and it will continue to actively reinforce control on waste handling practices by promoting sound waste management solutions to suppliers. Where our suppliers make products for other brands, the team will reach out to them to join the co-processing system. Moving forward, we will roll out this project to include also the Group's apparel and accessories and gear factories in Vietnam. The timeline here is expected to be late 2007 or early 2008.

#### **CO2 emissions from transport and travel**

The fuel used to transport goods to market creates carbon dioxide emissions, a major contributor to climate change. Our policy is to minimise the impacts from transport. Air travel creates the most CO2 emissions so is the focus of our efforts.

Carbon dioxide emissions are measured in grams carbon dioxide per kilometre each tonne travels (grams CO2/km t):

- Sea freight contributes 17.5 grams carbon dioxide CO2/km t
- Road freight by truck contributes 147 grams CO2/km t
- Airfreight contributes 903 grams CO2/km t.

In 2006, air freight transport was again driven and heavily influenced by a major global sports event, the FIFA World Cup™ in Germany. Selected time sensitive products had to be transported via air freight to meet customer requests.

See the Performance data section for the full breakdown of percentages of freight types used to ship adidas products.

#### **Offsetting the SEA team's travel impact**

As a global business, with over 150 locations worldwide and a global supplier base, air travel is widely used by adidas Group employees. As an internal project, the SEA team has recorded all their air travel activities in 2005 and quantified the respective carbon dioxide emissions as 342 metric tonnes. In 2006, the SEA team travel resulted in 421.4 metric tonnes of carbon dioxide. The increase in emissions is due to the greater number of team members running the Group's SEA activities around the world.

We are committed to fund a carbon-offset project which meets the quality standard defined by the World Wide Fund of Nature (WWF). This project will fund the construction of small local bio-gas facilities in Nepal, which help to improve the local infrastructure and living conditions through more safe sanitary conditions for the people, protecting the local wood and wildlife resources.

From 2007 onwards the adidas Group will regularly record global travel activities and will quantify respective carbon dioxide emissions. Approaches will be developed that encourage less air travel by setting feasible reduction targets.

### **Case studies**

In this section you can read how we have applied our approach on environmental issues to two particular factories in our supply chain. One case study looks at the gains made after implementing an environmental management system, and the other looks at tackling air pollution.

- Ongoing - Evervan factory, China, achieving much and inspiring others
- 2005 - Implementing environmental management systems in a football factory, China

- 2005 - Tackling air pollution in football production, Thailand

#### **Ongoing - Evervan, China, achieving much and inspiring others**

In passing the ISO 14001 in the year 2003 for the first time, and adapting our Guides of Best Environmental Practices, several initiatives and projects were finalised at the Evervan site, one of our major footwear suppliers in China, specifically:

- improved emissions, dust and noise control in work areas
- tighter management of chemicals
- replacement of diesel oil as the primary energy source in the canteen
- creation of a new waste management system
- an energy conservation project.

Energy savings were 15% for compressors, 21% for high energy devices such as mixers and rubber mills. A condensed steam recycling system saves 814 tonnes of water and 15.1 tonnes of diesel per month, paying for itself in 30 days.

Overall Evervan reported the following figures:

- saved water: 23.8% [ml/pair/month]
- saved electrical power: 2.68% [kWh/pair/month]
- saved diesel oil: 42.5% [kg/pair/month]
- saved gas: 47.6% [kg/pair/month]
- ratio of reused waste material: 47.6%.

In 2006 the following savings were reported:

- saved water: 53% [ml/pair/month]
- ratio of reused waste material: 68.8%.

#### **Apache II, China, learning from Evervan**

Results at Evervan have inspired other suppliers. For example, the new Apache II footwear factory integrated Evervan's findings into their new facility.

For 2006, the Apache II factory reported the following savings:

- saved electrical power: 9618.00 kWh/month
- saved diesel oil: 15.15 tons/month
- saved coal: 57.20 tons/month
- saved water: 1950.00 tons/month
- ratio of reused waste material: 45.8%

#### **2005 - Implementing Environmental Management Systems in a football factory, China**

Besides the high volumes of apparel and footwear products, China has become an important

production country for sports equipment, and in particular for footballs.

Saving resources is crucial to meeting business targets. Kuan Ho Sporting Goods Co, Ltd., one of our major manufacturing partners for machine-stitched footballs is located in Guangdong, China. The factory employs more than 6,500 workers and administration staff. The supplier has invested in Lean manufacturing and has made significant improvements to its workplace conditions and general health and safety. After some initial challenges the management committed to the SEA programme and Kuan Ho is now established as a long-term partner. They have developed a comprehensive HSE management system within the factory.

The supplier tackled their specific environmental challenges by working towards certification to ISO 14000 and OHSAS 18001, which they achieved in January 2005. There have been a number of specific measures taken.

#### **Environmental improvements**

Following our Best Environmental Practice Guidelines helped Kuan Ho to reduce average energy consumption by nearly 20% from 2004 to 2005 (from 1.70 KWh/Unit to 1.36 KWh/Unit) on single production units. These savings enabled the factory to reduce the amount of additional diesel needed by 53% on average.

The chemical storage room was completely rebuilt. Anti-leakage systems on the floors, an improved air circulation and exhaust system, and better management of the chemicals in the production rooms all minimised exposure for the workers. A new surface ionization system, instead of using solvents for cleaning, reduced the VOC (volatile organic compounds) emissions by about 80 Kg per day.

These measures not only reduced the site's environmental impact they also led to a 5% decrease in the product defect rate.

#### **Training and health surveillance**

Comprehensive HSE worker training sessions were conducted during the year, with 4,932 workers participating. A specific health check with 746 workers by an external medical service provider took place in April 2005. By implementing the HSE

system, occupational injuries reduced from 95 in 2004 to 50 in 2005.

#### **2005 - Tackling air pollution in football production, Thailand**

While the national legislation on health and safety and labour issues is clear, Thailand struggles to implement it. Government agencies tend to focus on the regulation of heavy industries. As many of the light industrial factories producing apparel and accessories are in zones dominated by heavy industry, they remain relatively low priorities for local safety inspectors.

#### **About the factory**

Molten Thailand Ltd has been a key ball supplier to adidas over the last four years. Molten and adidas have developed technology for new ball products including the Roteiro ball for the Euro 2004 Football Championships and adidas selected Molten as the main ball supplier for the FIFA World Cup 2006™.

Molten has 960 workers making branded and unbranded balls in two production buildings. The building producing branded balls for adidas is new and has good safety measures in place. The other older building, where non-branded products are manufactured, had major non-compliances with our standards, putting workers' health at risk. It did not matter that this was not the building where our products were made. We wanted to see our health & safety standards met across the whole site.

#### **Working together to address the issues**

In 2004, SEA and a local consulting firm, SERV Consulting, worked with Molten's management to curb critical problems with ventilation and chemical safety. Using our strategic monitoring approach to identifying root causes, the SEA team uncovered gaps in engineering control and worker awareness. SERV was subsequently invited to assess the company's Human Resource Management system and complete the training needs assessment.

Our standards focus on restricting the use of harmful substances. As a result we banned the use of toluene, a key ingredient in glue used for patching ball panels. This presented Molten with the challenge of meeting the same quality standards but with less toxic chemicals.

In July 2004, Molten's senior management committed to eliminating toluene and introduced other less harmful solvents. SEA monitoring

findings showed consistent efforts to improve ventilation systems and the factory management engaged a local chemical safety consultant and committed to ISO 14001 certification. In 2005, we provided training to Molten management and supervisors and Molten's safety team were trained in measuring against chemical thresholds. In September 2005, Molten had completely eliminated toluene from the production process at this site and was certified to ISO 14001.

**Improvements well received**

There is certainly more joint effort required to further improve the health and safety situation in Molten. However, the initiative of the past two years has clearly been a success:

*"In the past, I felt that adidas production plant was safer than my plant because of poor ventilation system. Now I feel that my production building has an improved working environment. Chemical usage is limited to only one-day supply, which relates to better ventilation." Worker's quote*

On the FIFA World Cup™, one worker states that: *"I am so proud of my country that we produce World Cup product. I think making World Cup Ball is more difficult than the Roteiro Ball but I take it as a challenge. I am proud to see them on the television and newspaper and I keep telling everyone that I am part of this special ball".*

## EMPLOYEES

Our people are crucial to our success. Achieving our goal to be the global leader in the sporting goods industry depends on the talents, enthusiasm and dedication of our employees.

Here we define our HR functions and goals, and our HR programme. We ensure worker-management communications through employee involvement in decision-making. The employees have a responsibility to adhere to the employee code of conduct; and as employers we have a moral responsibility to ensure their health and safety. This includes developing an HIV-AIDS policy. The way we reward our staff has to be fair and related to our, and their, achievements.

We aim to develop our employees with opportunities for career progression, while striving to create a climate that celebrates our diversity, promotes global mobility and helps our staff achieve a healthy work-life balance. We also offer our staff access to a wide range of company sports activities.

### HR functions and goals

HR management is a core function within the Group's global organisation, managed by Global HR, with the global director reporting to the CEO. Within the Group, the Global HR organisation manages the following key functions:

- HR management and support to key functions – Global Operations, Global Marketing, Corporate Services, Regions and Brands
- Global Services, including reward management and mobility management
- training and development
- company sports programme and work-life balance initiatives in Germany
- corporate community programme in Germany
- cross-functional issues, for example, HR information systems, communication, personnel and marketing.

Global HR focuses on the following goals:

- to create a working environment that stimulates team spirit, passion, engagement and achievement
- to instil a performance culture based upon strong leadership
- to make the adidas Group the employer of choice.

### HR programme

Our people and their talents are critical to our continuing commercial success. With more than 27,000 employees working at more than 150 locations in more than 50 countries we need to develop HR strategies that can be implemented globally. The first step is to identify the common challenges we face wherever we operate:

- talent management – to identify, recruit and retain the most talented people and develop career opportunities for them tailored to the specific needs of our company
- employee-oriented leadership – to strengthen the alignment of management and employees by improving communication and enhancing employee feedback systems
- performance management – to instil a result-driven management culture that supports up and downward performance feedback for continuous learning and improvement
- motivation – to provide reward and incentive schemes as well as a working environment that promotes employees' commitment, engagement and wellbeing
- communication – to improve transparency and efficiency in communication at all levels of the Group and wherever we operate.

To rise to these challenges, our programme focuses on five core processes of HR management: attracting, recruiting, developing, rewarding, and retaining staff.

## Employee involvement

Employee empowerment, participation and co-determination play an important role in managing employee relations within the adidas Group.

The Group has established works councils at adidas in Germany and other European subsidiaries. The members of the work councils are elected by the work force.

Currently, three representatives of the works council are also members of the Supervisory Board. The Supervisory Board advises and supervises the Executive Board in the management of the adidas Group. It is involved in all decisions of fundamental importance to the Group and is responsible for appointing and dismissing members of the Executive Board.

Location determines the form of employee participation:

- HQ Works Council
- European Works Council
- Employee participation outside Europe

### HQ Works Council

In 2006, the HQ works council focused on the following projects:

- Job-grading and Performance/Compensation System (PEP)
- Work-Life Balance/Family Audit
- Annual performance bonus for eligible employees
- Internal agreements on the use of internet, (mobile) phone and E-mail, on reintegration of employees coming back from parental leave, and on on-call service.

### European Works Council

The European Works Council (EWC) currently consists of nine delegates from six European countries. The fruitful collaboration between the European and HQ Works Council and the SEA team continued in 2006. Members of the HQ Works Council, the European Works Council and representatives of the Trade Unions are regularly updated on progress of the compliance programme.

### Employee participation outside Europe

While employees of the adidas Group in Herzogenaurach and Portland have enjoyed access to top management in a variety of forums, creating effective communication channels throughout the regions at Liaison Office (LO) and factory level is a constant challenge.

Our internet-based 'Ask the Management' forum gives employees throughout the regions an opportunity to raise concerns and post questions to top management. More direct communications are being established in the sourcing offices throughout Asia, based on the Guangzhou model detailed in our Social and Environmental report 2003. The Guangzhou management-employee committee is now in its fifth year and has incorporated elected representatives from Apparel, Accessories and Gear as well as the Originals footwear sourcing representatives.

Since its establishment, this committee has discussed and in most cases resolved a number of key issues, including:

- organising transport to our operations centres
- providing medical insurance for staff located in different cities
- improving the housing accumulation fund and social retirement fund coverage
- introducing flexible working hours in the LO
- choosing the venues and activities for company outings.

The committee is about to be restructured in order to accommodate representatives from Reebok Operations staff.

## Employee code of conduct

We have a Group-wide Employee Code of Conduct to help strengthen general governance. The Code serves as the cornerstone of ethical and social behaviour in day-to-day operations, and is aligned with the core values of the company.

In 2005, the code was subject to a detailed review. The revised version was released in 2006. The code is part of a Global Compliance Programme and is planned to be implemented by compliance managers worldwide, with the involvement of the Works Council.

The code covers key issues such as:

- Treatment of business partners and third parties
- Handling of information
- Complaints
- Special rules for dealing with financial matters.

## Health and Safety

Everyone has the right to work in a safe environment. This has been recognised the world over and as a global Group, our operations have to comply with a wide range of different legal and cultural imperatives. Naturally, practices and procedures will vary from one facility to another, but the core requirements remain the same.

These core requirements are fully explained in a set of Corporate Guidelines for Health, Safety and Environment for facilities of the adidas Group. These guidelines especially help facility management of mainly administrative offices to manage health and safety issues in an effective way. Furthermore, larger administration facilities of the adidas Group and the very few production sites owned by the Group have comprehensive risk, health, safety and environmental management systems coordinated by local facility management. Key subjects of the Group's health and safety management are also activities focused on travel security and health and safety and precautionary measures related to communicable diseases like avian flue and SARS.

## HIV-AIDS policy

Based on guidance materials issued by the ILO and comprehensive field-testing by the adidas Group Liaison office in Thailand, the adidas Group launched a Group-wide HIV-AIDS policy in 2006. The policy contains general guidance on HIV-AIDS, an employee guide, and guidelines for HR managers on workplace care and support.

The policy was subject to review by the company doctor who proposed improving the privacy and confidentiality measures in the reporting mechanisms.

## Remuneration

Our Global Salary Management System (GSMS) sets employees' salaries in a clear, understandable and measurable way. It relates to performance evaluation and uses a clearly defined system for setting salaries in line with market requirements and performance levels. Managers and the HR department can evaluate where each employee currently is within the system based on his/her current salary and where he/she should be. The adidas Group also offers several attractive variable compensation components:

- Pay for Performance bonus programme - More than 20% of all employees receive this variable salary component with an average of 20% of their remuneration linked directly to individual and Group performance.
- Long-Term Incentive Programmes (LTIP) - These include brand- or business-specific three-year plans for senior managers that are based on the achievement of financial as well as compliance targets.
- Management Share Option Plan (MSOP) - Beneficiaries of the MSOP (members of Executive Board and senior management) may exercise stock options granted to them in five tranches since 1999 if at least one of two performance criteria is met.
- Other benefits include our 401-K pension plans in the USA and the PP 2000 pension plan for our employees in Germany. In 2006, 1,154 employees participated in the latter, which represents an increase of 7% compared to the previous year.

## People management

We aim to identify, recruit and retain the best people by providing development and career opportunities on a Group-wide level. We achieve this through our strategic HR pillars that focus on:

- creating a positive work environment
- instilling a culture of performance
- and being the employer of choice.

### Go for Gold

Just like athletes, employees of the adidas Group need a training plan and a coach to build on their strengths, overcome their own challenges and improve their technique to achieve their goals. We 'Go for Gold' and base our efforts on the three success drivers of our performance culture:

'Leadership Excellence', 'Performance Management' and 'Talent Management'.

### Leadership Excellence

Leadership in what we do and how we do it is key to our success. Our Executives and Managers enforce Leadership Excellence and instil a culture of performance. They are the main drivers and sponsors of the company's Performance and Talent Management.

### Performance Management

Performance Management is the platform of our success. Evaluation tools like PEP ('Performance Evaluation and Planning') measure employee's current performance based on job and competency requirements. Employee performance levels serve as an indicator for base salary development and variable compensation, supporting our goal of paying for performance. PEP also covers the setting of individual business targets and the planning of training and development activities. For both individual and team performance improvement we offer targeted support based on need: for example, basic skill training in team development or business coaching. All aiming for one goal: to train and develop our employees to be 'Fit for Today'.

### Talent Management

With our Talent Management tools and processes we identify employees at all levels who have the potential to become leaders in the business - our Talents. In order to prepare them for new and more complex future roles they take part in targeted development programmes covering:

- innovative and state-of-the-art input in the area of management and leadership
- individual preparation for new competency requirements
- fostering of global networking
- knowledge transfer into the current and future business.

Actively managing internal succession is key to our competitive position.

## Diversity

Over the years, the workforce of the adidas Group has evolved to reflect the growing diversity of our communities, our varied fields of activity as well as our truly global marketplace. We will remain committed to understanding, valuing and

incorporating this diversity into the corporate culture of the adidas Group.

We believe that diversity helps us to sustain a competitive advantage, to foster motivation and to ensure organisational success and stability. Our approach to diversity is to:

- **Acknowledge** the richness of commonalities and differences we share; the intrinsic worth of each unique employee; that our products and our contribution to sports and the athletes that compete therein are enhanced through these multiple and different perspectives;
- **Aspire** to create respect for and appreciation of each other; to further increase diversity within the adidas Group and to foster a spirit of openness and partnership amongst our employees and within our communities.
- **Act** to assure an environment that welcomes, respects and embraces diversity; to capitalise on the value of a diverse work force; and to achieve excellence through our products and our people.

## Global mobility

Global presence and success in worldwide markets require a workforce willing and able to work around the world. For those employees who are interested in working in different countries, we have a programme of international assignments to worldwide locations within the adidas Group. Most of these take place between Germany, USA, China, Hong Kong and The Netherlands. The adidas Group provides training and cultural preparation to familiarise the relocating professionals and their families with their new living and working environments. In brief:

- the Headquarters of the adidas Group employs more than 500 international employees from almost 50 countries
- between 100 and 150 international assignments at various locations begin annually
- about 450 employees are currently on international assignments.

## Work-life balance

Every employee's quality of life should be improved by working for the adidas Group. So we have a responsibility to address work-life balance. We aim

to harmonise the commercial interests of the adidas Group with the private and family needs of our employees, thereby assuring the mutual benefit of both. The programme includes family oriented services, flexible work time and place, people development and leadership competence related to work-life balance. More information about this topic can be found in the Employees section of our website.

Hertie Stiftung, the third largest private foundation in Germany, audited our programme to identify and initiate ways to improve family-oriented personnel management. We were re-audited in 2004 and awarded the official certificate as a Family-Friendly Employer.

## Company sports

We offer our employees a wide range of sports activities at our major sites including team sports such as football and basketball, fun and fitness courses such as fencing and Tae Bo, and health and wellness courses such as yoga, healthy back, and swimming.

At our Headquarters in Herzogenaurach, Germany, our Company Sports department also organises several sports events such as mountain biking, horseback riding, kayaking, skiing and ski tours and the biathlon. Special events such as one-week sports camps for employees' kids, transalpine mountain bike tours, and the yearly Berlin marathon weekend (with a suitable training programme prior to the event) are also available.

At our Headquarters in Herzogenaurach and Portland our employees have access to a company gym.

## COMMUNITY AFFAIRS

In managing our community affairs programme the adidas Group has adopted a largely decentralised and brand-oriented model for community involvement practices, recognising that people in our regional subsidiaries and Group entities best understand the needs and cultural sensitivities of their local communities. At the Group level we support our suppliers' communities, as well as make contributions to organisations that promote sustainable development practices within the industry.

Although varied in form, the initiatives are all aimed at supporting children and young adults, with sports as a common theme. We have three complementary pillars supporting our community affairs goals: community involvement, employee involvement and corporate giving and we list examples in these sections. Some initiatives are described in more detail under case studies.

### Managing community affairs

We want our community affairs work to be as innovative as our efforts to improve workplace conditions. To achieve that we have first clarified internal ownership:

- Internal Group activities are overseen by a network of employees from around the business. This network is coordinated by Community Affairs, a function that has been fully embedded in the Social & Environmental Affairs Department.
- External supply chain activities are managed by the Social and Environmental Affairs (SEA) team directly.

#### Group activities

##### *Developments*

In 2004 we established the Community Affairs function at Headquarters as part of the Social and Environmental Affairs team in order to develop a direction and strategy for Corporate Giving and other Community Involvement practices. Since 2005 we have been focusing on working with a network of people from adidas Group entities around the world who are driving social improvements in their local communities.

Community Affairs provides support and assistance to them, especially when they are seeking advice on important projects. The challenge with our decentralised and brand-oriented approach is to implement comprehensive reporting mechanisms

so we can form a clear view of activities at the local level, and better analyse and report on them.

In 2006 we were able to improve our existing reporting mechanisms. Nevertheless, it remains a challenge for our reporting to be truly comprehensive and we still have some way to go. At Group level we continued to support our suppliers' communities, as well as make contributions to organisations that promote sustainable development practices within the industry.

##### *Next steps for 2007*

After the integration of Reebok we are now in the process of reviewing our Community Affairs strategy at a Group level and plan a stronger focus on community and social programmes in the countries where our suppliers are based. In those countries where adidas Group entities and our suppliers both run social programmes, we will keep on building links between the two with the goal of increasing the programmes' impact.

##### *Pillars of the programme*

The adidas Group Community Affairs programme is built on three pillars: community involvement, employee involvement and corporate giving. In each community the specific design of these three pillars is determined by local cultural, economic and social factors. We are selective and support projects that show sustainable benefits to the communities where we live and work.

**Supply chain activities**

Many of our suppliers are involved in local projects that are valued by their communities. However, we are aware that we could achieve much more. Working with Marie Stopes International in Vietnam or supporting the Sudhaar education project in Pakistan has helped us to see that the adidas Group can act as a catalyst for change – change that would

otherwise not occur – by partnering with a capable third party and our suppliers on a specific community and worker-oriented social programme. We will continue to support suppliers' communities as well as to make contributions to organisations that promote sustainable development practices within the industry.

**Initiatives**

Examples of initiatives taken by the Group, its entities and subsidiaries around the world include:

	Europe/Middle East/Africa	Asia-Pacific	Americas
<b>Community Involvement</b>	<p>Ongoing - 'Impossible is nothing' - cause-related marketing initiative, adidas Italy</p> <p>Ongoing - 'Franconian International School' Community Involvement, adidas Headquarters Germany</p> <p>Ongoing - 'Diambars' Community Involvement, adidas France and Senegal</p>	<p>2006 - 'Fundraising for Caring for Children Foundation', adidas Hong Kong</p> <p>2005 - 'JinQiao 8K Running event' - Grassroots Community Project, adidas China</p> <p>2005 - 'Tsunami Relief Efforts', adidas Korea</p>	<p>Ongoing - 'Junior Achievements' - educational programme, adidas Panama</p> <p>Ongoing - 'Earn your Stripes' Scholarship Program, adidas America</p> <p>Ongoing - 'Golf Fore Your Heart Pro-Am Tournament', TMaG Headquarters, US</p> <p>Ongoing - 'Terry Fox' cause-related marketing project, adidas Canada</p> <p>Ongoing - 'New Orleans Recovery Effort', adidas US</p> <p>2006 - 'Association ALE IAP' cause-related marketing activity, adidas Mexico</p>
<b>Employee Involvement</b>	<p>Ongoing - 'Kids Sport Fun Day', adidas Headquarters, Germany</p> <p>2005 - 'Blood donation' from employees, adidas Dubai</p>	<p>Ongoing - 'adiLIFE' Corporate Volunteering Programme, adidas Australia</p> <p>Ongoing - 'Special Olympic' Corporate Volunteering and Product Giving, adidas Japan</p> <p>2006 - 'adidas Soccer Clinic', adidas Japan</p> <p>2005 - 'UDAYAN Care' Corporate Volunteering, adidas India</p>	<p>Ongoing - 'aCT!' adidas Community Team, adidas America</p>

<b>Corporate Giving</b>	Ongoing - 'Product Donations', adidas Spain	2006 - 'Product Donations', adidas Singapore	Ongoing - 'Charitable Contributions Program' TMaG Headquarters, US
	2006 - '6 villages for 2006' Cash donation, adidas Headquarters Germany and South Africa	2006 - 'Children's Day DongA Daily Quiz Event', adidas Korea	Ongoing - 'Product Donations to children and disabled', adidas Argentina
		2005 - 'Cash Donation to orphanages', adidas Liaison Office Indonesia	2006 - 'BELL Foundations', Reebok Foundation US

## Community involvement

Community involvement for us ranges from conventional community projects and cause-related marketing initiatives to immediate relief efforts for people in need.

### Cause-related marketing initiatives

The adidas Group joins with charities or good causes to market products that make a positive impact on key social issues and achieve business objectives.

### Relief efforts

The adidas Group responds to natural disasters around the globe, for example the Tsunami in South-east Asia, Hurricane Katrina in the US and the earthquake victims in Pakistan.

Read about community involvement initiatives in our three operating regions:

- Europe/Middle East/Africa
- Asia-Pacific
- Americas

### Community involvement in Europe, Middle East and Africa

#### Ongoing - 'Impossible is nothing' cause-related marketing initiative, adidas Italy

adidas Italy brought to life our campaign 'Impossible is nothing' by creating opportunities to participate in sport where none had previously existed. In 2005, ten Italian cities were chosen. For example, the floor of the prison gymnasium in Monza was laid, and a fencing piste for the Nisseno Fencing Group of Caltanissetta was supplied.

#### Ongoing - 'Franconian International School' Community Involvement, adidas Headquarters Germany

The Franconian International School, close to the adidas Headquarters, has approximately 150

students from more than 20 different ethnic backgrounds. It aims to educate their students in an international environment to high academic standards and to create an atmosphere and spirit that respects all cultures and promotes responsible citizenship. Since it opened in 1998, many employees of the adidas Group have enrolled their children here and the company has been involved in all aspects of school life and management.

#### Ongoing - 'Diambars' Community Involvement, adidas France and Senegal

The Diambars initiative has been developed by a group of professional football players in France and establishes sports schools for children from the African continent. The Diambars adidas Project aims to support the training of sports people, to contribute to the development of mass sport in Senegal and promote the value of learning and education. In 2005, a highlight was the pupils' summer school visit to adidas France in Landersheim. Supporting the initiative since the very beginning, adidas France remains the key enabler of the project with adidas France employees being closely involved in the development of the kids from Senegal.

### Community involvement in Asia-Pacific

#### 2006 - 'Fundraising for Caring for Children Foundation' event, adidas Hong Kong

Aiming to benefit kids and youth volunteers the adidas Hong Kong joined a half-day event in order to raise money for children in need. In addition, adidas sponsored products for a charity sale.

#### 2005 - 'JinQiao 8 K Running Event' Grassroots Community Project, adidas China

adidas China is the title sponsor of the JinQiao 8 K running event held at JinQiao community in Pudong of Shanghai. We promoted healthy living through building up a grass roots running community from

the event. A total of 1,489 people participated in the run.

**2005 - 'Tsunami Relief Efforts', adidas Korea**

With the objective to play a role as a global citizen, adidas Korea donated to UNICEF. The aim was to support the organisation's relief efforts in meeting the humanitarian challenges after the Tsunami in Indonesia. We decided to collaborate with UNICEF in order to effectively direct relief funds to those most affected by the disaster. The company decided to match employee donations in order to reinforce individual personal commitment while acting as a socially responsible company.

**Community involvement in the Americas**

**Ongoing - 'Junior Achievements' educational programme, adidas Panama**

Since 2001, in collaboration with Jóvenes Emprendedores adidas Panama has been promoting understanding of the development of a global economy for children at elementary school and high school. The main goal is the formation of leaders within a business culture from an early stage by educating and inspiring the youth so that they value free enterprise and understand the global economy and the world of business. adidas Panama supports this project not only through corporate giving but also through employee involvement.

**Ongoing - 'Earn Your Stripes' Scholarship Program, adidas America**

Since 2000, the adidas America 'Earn Your Stripes' Scholarship Program annually awards 17 financial scholarships to high school seniors from Portland public schools, who demonstrate their commitment and achievement in the areas of academics, athletics and community service. In addition to the financial award, each recipient receives a college kit that includes our product and school supplies.

**Ongoing - 'Golf FORE Your Heart' Pro-Am Tournament, Taylor-Made adidas Golf, Headquarters US**

The TaylorMade-adidas Golf 'Fore' Your Heart Pro Am has become the largest local charity golf tournament supported through TMaG Charitable Contributions Program.

TMaG provides product for all levels of team prizes and for individual putting, most accurate drive and long drive contests. At the evening's live auction, a gift certificate is auctioned to the highest bidder for

the opportunity to be custom fit for a set of clubs designed to his or her swing specifications.

We also provide a \$15,000 purse for the annual Pro-Am, which is held in conjunction with the tournament. PGA professionals throughout Southern California are paired up with four tournament participants to compete in this spectacular one-day event.

**Ongoing - 'Terry Fox' cause-related marketing project, adidas Canada**

adidas Canada and the Terry Fox Foundation partnered in order to introduce the iconic indigo blue shoe, the adidas Orion TF. All profits of the sale were donated to the Terry Fox Foundation.

Terry Fox was a Canadian runner, who set out to fight cancer that had taken one of his legs. His goal was to raise money for cancer research by running through Canada from east to west, calling his journey the 'Marathon of Hope'. Fox was forced to quit after 143 days of running when his cancer returned, however, along the way he raised the awareness of people around the world. Today, the Terry Fox Foundation remains true to Terry Fox's vision and principles while raising money for cancer research through the annual Terry Fox Run, donations and planned gifts. During this run, Fox wore his favourite running shoe, the 1979 adidas Orion, which adidas provided him with in 1980.

This is the first time the Terry Fox Foundation has partnered with a corporate organisation. On an annual basis adidas Canada will explore with 'The Terry Fox Foundation' tasteful marketing initiatives that meet the three objectives of:

- raising awareness for the Terry Fox Foundation
- increasing participation in the annual run, and
- raising funds for the Foundation.

**Ongoing - 'New Orleans Recovery Effort' Relief effort adidas, US**

In collaboration with the NFL and the adidas sponsored athlete Reggie Bush we help in the recovery efforts in New Orleans following the devastation of Hurricane Katrina. adidas and Reggie Bush combined resources to make a significant financial contribution to restore the Holy Rosary Academy/High School and to refurbish the facility and field at Tad Gormley Stadium in New Orleans City Park, also severely damaged in the storm.

**2006 – 'Association ALE IAP' cause-related marketing project, adidas Mexico**

adidas Mexico donated profits generated through selling an accessory tag in our own retail stores to the Association ALE IAP medical fund. These donations supported carrying out transplants of organs for socially deprived people who cannot afford such surgery or have no access to Mexico's Medical Social Security.

**Employee involvement**

Employee involvement supports the company's community affairs goals and objectives by providing meaningful opportunities for our employees to engage with the communities where they work, and may also live. Read about employee involvement initiatives in our three operating regions:

- Europe/Middle East/Africa
- Asia-Pacific
- Americas

**Employee involvement in Europe, Middle East and Africa**

**Ongoing – 'Kids Sport Fun Day', adidas Headquarters, Germany**

The Kids Sport Fun Day aims to help social deprived kids find friends by joining collaborative activities that enhance their self-esteem through sport. The kids spend a whole day playing sports and games and having fun at the adidas Headquarters in Germany.

Another element to the Kids Sport Fun Day is that almost the whole project management is in the hands of adidas apprentices. On a voluntary basis they have the chance to plan, execute and follow up this event as they see fit.

The 2006 event was very successful and therefore will be repeated in 2007.

**2005 - 'Blood donation' from adidas employees, adidas Dubai**

The Blood Donation Vehicle, provided by the UAE Ministry of Health was with adidas Dubai for one day and after a slow start, and some uncertainty and nervousness, people began to filter into the Blood Donation Vehicle. Even though going through the unpleasant task of giving blood, we bonded with our office neighbours, who joined in from the street, and had a worthwhile, rewarding day.

**Employee involvement in Asia-Pacific  
Ongoing - 'adi-LIFE' Corporate Volunteering Programme, adidas Australia**

adidas Australia embraces social responsibility and actively commits to benefiting the Australian community through support and involvement in sport.

Every employee can become an adi-LIFE volunteer in order to:

- create and participate in volunteer activities that improve communities
- promote education
- promote physical activity through sport
- seek out other motivated adi-LIFE employees to become volunteers to share common experiences and the camaraderie of everyone with whom we work.

**Ongoing - 'SPECIAL OLYMPICS' Corporate Volunteering, adidas Japan**

The Special Olympics is an international organisation that offers children and adults with intellectual disabilities the opportunity to participate in society through sport.

We feel the Special Olympics convey adidas values of passion, authenticity and honesty in sport. adidas feels that the funding money is important, but the volunteer spirit of adidas staff is even more important for successful community programmes and therefore, since 2005, adidas employees have supported the event through volunteering activities.

**2006 - 'adidas Soccer Clinic', adidas Japan**

adidas volunteers and a football coach visited an orphanage in Tokyo and taught the children to play football in order to convey to them the essence of team spirit and fun in sports. In addition, adidas Japan contributed uniforms and footballs to all the children.

**2005 - 'UDAYANA CARE' Corporate Volunteering, adidas India**

India is a poor country. Our management team wanted to give something back to the community and has joined hands with UDAYAN CARE, a registered charity working with orphaned and abandoned children. Our mission for helping the disadvantaged kids is to:

- create a mentoring environment by involving staff
- providing financial assistance in-kind.

We invite these children to our office on weekends to spend some fun time on sporting activities. This includes coaching and mentoring by the staff.

Udayan care has four homes in Delhi that support 80 kids. These are residential homes for long-term care of disadvantaged children through a programme called L.I.F.E: Living in Family Environment. Women of vision volunteer to set up and sometimes even fund these homes and parent the children. These homes are in busy, middle class neighbourhoods, where the community takes ownership of them.

**Employee involvement in the Americas  
Ongoing - aCT-adidas Community Team, adidas America**

As part of the Company's commitment to improving the communities in which we operate, adidas America has developed an employee volunteer programme called aCT! aCT! is the adidas Community Team, an employee volunteer programme that encourages employees to extend the adidas brand values of commitment and inspiration to helping those in our community reach their potential. Employees receive time away from work to help in the community by volunteering with non-profit community partners. Employee volunteer efforts are recognised with a financial contribution to the community partners when accumulated employee volunteer hours reach a total of 60 hours per six-month period. The programme was launched in autumn 2005 at an on-site volunteer event at the adidas Village (US Headquarters) in Portland where the programme will be piloted throughout 2006.

**Corporate giving**

Donations at the adidas Group can take the form of financial contributions, product contributions and in-kind goods and services. Globally, in 2006, the adidas Group received 10,702 donation requests, supported 166 requests with a cash grant and 1,137 with product donations. For more information see the Performance data section.

Read about corporate giving initiatives in our three operating regions:

- Europe/Middle East/Africa
- Asia-Pacific
- Americas

**Corporate giving in Europe, Middle East and Africa  
Ongoing - 'Product Donations', adidas Spain**

adidas in Spain donates products to various social service organisations, including the Spanish Special Olympics, SOS Children's Villages in Spain and an Orphanage in Jaen. Furthermore, product donations were sent to Nicaragua and Indonesia to help people in need.

**2006 - '6 villages for 2006' Cash donation, adidas Headquarters Germany and adidas South Africa**  
Please see case study for more information.

**Corporate giving in Asia-Pacific  
2006 - 'Product Donations', adidas Philippines**

adidas in the Philippines donated products to a variety of Foundations benefiting the need in their local community.

**2006: 'Children's Day DongA Daily', adidas Korea**  
adidas Korea donated mini balls to children participating in a quiz event celebrating the children's day in Korea.

**2005 - 'Cash Donation to orphanages', adidas Liaison Office, Indonesia**

Several Indonesia Liaison Office employees and their families visited five orphanages between July and September 2005 to distribute money that was raised in an internal sample sale. The employees spent some time with the orphans there.

**Corporate giving in the Americas  
Ongoing - 'Charitable Contributions Program' Taylor-Made adidas Golf, US**

TMaG receives a vast amount of requests for donations – an average of 3,000 annually and therefore, developed the 'Charitable Contributions Program'.

Along with donating products, the Charity department offers the sale of TaylorMade-adidas Golf products to qualified charities at a discounted fee of up to 20% below wholesale pricing. A portion of the profit generated by the sale is donated back to the charity in the form of additional products. The remaining profit is applied to the cost of running the programme, including wages and benefits for two full-time employees and one part-time employee, with the remaining balance contributed to TMaG at year-end. The end result is a totally self-funding programme designed to create a win-win proposition for everyone. The charities are able to raffle, auction or use the product they've purchased

to raise funds that easily eclipse the price charged by TaylorMade and the charity programme has completely covered all of its costs.

Since its inception in 2001, TMaG's Charitable Contributions Program has grown in popularity and leads the industry with this innovative approach. The programme allows us to enjoy a larger presence at a greater number of fundraising events, spreading goodwill for TMaG throughout the country year round. Our willingness to partner with charities has proven to be highly valued across the nation, resulting in strong brand loyalty among thousands of golfers, their families and friends.

**Ongoing - 'Product Donations for children and disabled', adidas Argentina**

adidas Argentina donates products to various social organisations in order to help groups in the community that cannot acquire this type of product. The focus was children and the disabled.

**2006 - 'BELL Foundation', Reebok Foundation, US**

The BELL Foundation (Building Educated Leaders for Life) began in Boston in 1992 and soon became a programme that was expanded to other major cities in the USA. BELL's mission is to increase the educational achievements, self-esteem and life opportunities of elementary school children, kindergarden through 6th grade, living in under-resourced urban communities through after-school and summer programmes. The vision of BELL is centered in the basic premise that all children can learn when they are nurtured and taught by knowledgeable and caring adults who believe in them and are committed to their growth.

The Reebok Foundation partnered with BELL in a 3-year grant to assist in the strategic expansion of the BELL programme into new urban centres in the USA bringing the number of students participating from 1,300 to 7,500. The goal is to serve 10,000 children in four to five metropolitan areas by 2007.

A grant from the Reebok Foundation allowed BELL to expand this national programme into markets where Reebok has a presence. The goal of the strategic initiative was to achieve dramatic growth while increasing programme impact on children's lives.

**Applying for a grant**

In 2005, we developed Guidelines on Corporate Giving so we could help the applicants, better

manage the large number of donation requests and remain true to our values in the approval process. In the guidelines we defined areas where we would and would not get involved, the application procedure and grant requirements.

You can find our Corporate Giving Guidelines in the Community affairs section of our website.

Organisations seeking support should send their request to the subsidiary or Liaison Office in their home country or the closest office. More information about office locations is available on our website in the About us section.

**Case studies**

Here we describe some of our initiatives in more detail:

- Ongoing - Reproductive health project with Marie Stopes International
- Ongoing - Sudhaar education and school infrastructure programme, Pakistan
- Ongoing - adidas America and football (soccer)
- 2006 - SOS Children's Villages

**Ongoing - Reproductive health project with Marie Stopes International**

**The project so far**

In 2003, we reported on our developing partnership with Marie Stopes International (MSI). Based on the research and survey work that was conducted at supplier factories in Vietnam in the first quarter of 2004, a broad-scale project aimed at addressing the fundamental sexual and reproductive health of workers has been developed. During the survey and research phase, it became clear that the two fundamental problems for workers are:

- Lack of knowledge and awareness in relation to managing their own health
- Lack of access to reproductive medical services.

Research and survey work has also started in Dongguan in south China, to assess the needs of workers, factory management and local authorities in respect of reproductive health amongst the largely migrant workforce.

**China programme**

In 2004, the Chinese authorities fully acknowledged the growing impact of HIV-AIDS. Given the growing support for programmes that address the

increasing health risks for China's urban workforce, the MSI China programme will identify the best methods for protecting workers against this disease and poor reproductive health in general. Underpinning the programme is the concept of personal responsibility.

At relatively minimal cost to factory management, a significant number of workers can effectively be taught how to protect themselves and improve their overall health and wellbeing.

During the course of 2005, MSI was heavily involved in the roll-out of several critical projects relating to HIV-AIDS in Yunnan, one of the provinces with the highest rate of infection in China, and the opening and development of its new China MSI clinics. Nonetheless, we still managed to convene a workshop at the adidas offices in Guangzhou, facilitated by MSI, to bring the relevant stakeholders together for the purpose of reviewing the needs assessment conducted at two different suppliers. We received feedback from the factories, the Guangdong Bureau of Health, the Family Planning Association, the China CDC, and experts from the Migrant Labour Research & Service Center of Zhongshan University and the Guangdong Women's College.

Following the workshop, both MSI and adidas have been conducting outreach with a number of different organisations to enlist their participation, in order to make this a truly multi-sectoral, private-public engagement. A proposal has been submitted by MSI for a programme covering the needs of workers in Guangzhou and Dongguan, with the potential to reach thousands of factories and 100's of thousands of workers. At this stage, there is some possibility that the programme may be pursued under the umbrella of the China Health Alliance, through the efforts of the Global Health Initiative.

#### **Vietnam programme**

In January 2005, the implementation phase of the Vietnam programme started, with the establishment of a permanent reproductive health clinic to service workers and the surrounding communities. In addition to this, a mobile team travels out from the clinic to the factories to provide a range of services including training of factory clinic staff, basic reproductive clinical services, distribution of information and educational materials, and direct training of volunteer workers as peer group leaders.

MSI has built capacity for the factory medical staff in basic counselling on contraceptives and essential reproductive health care through counselling training. Post training supportive monitoring has been conducted to ensure knowledge and skills obtained are put into use. Advocacy work is being done targeting at the senior management of the factories to make contraceptives easily available and accessible by the factory workers.

Marie Stopes also assist factory clinic staff to develop a proper referral network with local clinics, hospitals and pharmacies, as well as promote the MSI clinic and its unique philosophy on health services and standards. This activity makes it easier for the factory workers to access information and services on sexual reproductive health including HIV/AIDS prevention education.

Privacy, confidentiality and counselling of the patient or client are still somewhat novel concepts in Vietnam.

*'MSI and adidas share a common vision that solutions must be long term, sustainable and cost effective, with direct benefit for factory workers as well as factory owners.'* Marie Stopes International

By the end of 2005, the MSI static clinic had been operating effectively in Binh Duong province for several months with numbers of factory worker clients far exceeding expectations. Several short documentary news-items and public service announcements by local authorities and media helped raise awareness about the clinic and the need for these types of services to be made more readily available to migrant workers. Local authorities in Binh Duong province have been extremely cooperative and supportive of the clinic, ensuring smooth operations, and this was mostly due to the excellent government relations conducted by MSI.

At the same time, the MSI staff in Ho Chi Minh City has been working with all individual suppliers in each of the three product categories (footwear, apparel and accessories & gear) to map-out activities and timelines for their factory clinic staff training and peer education programme roll-out. As the result of the annual review meeting in March 2006, adidas and MSI agreed on and start tracking a number of key success indicators and other useful information, such as: number of local community clients versus factory clients accessing the static

clinic; rate of use of mobile services versus use of static clinic by factory workers; the general health status of clients as well as other critical information, e.g. education level, current living conditions; and sick leave or absences from the factory due to gynaecological or hygiene problems or unwanted pregnancy. It is also anticipated that other buyers and donors may be brought into the programme to extend its impact.

#### **Developments in 2006**

In mid 2006, there was a quick assessment of the Peer Educator Programme conducted to identify areas of improvement for the programme. The programme generally runs well with vital participation by the 443 Peer Educators who are the direct workers from factories. 8,940 workers were provided with information on contraceptives and essential reproductive health issues by trained Peer Educators. They also referred 1,362 workers to the static reproductive health clinic and 8,601 workers met the mobile team for information and services.

A strategic planning section was conducted with all senior managers of the factories during which issues of concerns and barriers were presented and discussed in January 2007. As a result, the senior management committed to a strategic plan to facilitate Peer Educators and Factory medical staff to provide Sexual Reproductive Health information and contraceptives to workers right at the factories.

The project was also visited by government officials from the Ministry of Health in Vietnam and the representative of the United Nations Population Fund in Vietnam. The project attracts a lot of attention from central and local government agencies and international organisations. Other surrounding non adidas factories approached the project to request that similar activities be undertaken with their workforce. The static clinic was also visited by Mr. Luong Van Cu, the Vice Chairman of the Committee for Social Affairs in the Vietnam National Assembly in March 2007. This visit resulted in a call for a meeting with local government agencies in Binh Duong where the static clinic and the companies working in the province are located. The meeting is scheduled for June 2007 and will discuss how the government of Vietnam, the private sector and NGOs can work in partnership to replicate the model being piloted by adidas and MSI in Vietnam.

UNFPA (United Nations Population Fund) have suggested to MSI Vietnam that they could provide technical assistance to the district governments in Hanoi and Ho Chi Minh City about implementing an intervention programme targeted at migrant youths based on the proven success of the adidas/MSI initiative.

Due to the positive results of the project, MSI Vietnam has received a grant from the European Union to integrate the Voluntary and Confidential Counselling and Screening test on HIV (HIV VCCT) into the MSI Binh Duong clinic. This means that the service is now available to the factory workers in Binh Duong and Ho Chi Minh City. It is the plan that the Peer Educators will be trained specifically on HIV/AIDS prevention education and the factory medical staff will be trained on HIV VCT counselling as well.

#### **Ongoing - Sudhaar education and infrastructure project, Pakistan**

Sialkot is the centre of the football stitching industry in Pakistan, which has in the past employed underage workers. To discourage this, standards of education and access to schooling have had to be improved in rural communities in the area, which is what the local NGO Sudhaar has done with its Education and School Infrastructure programme. Originally supported by FIFA, the adidas Group has fully funded the programme since 2002.

Sudhaar has successfully motivated parents to keep their children in school, developed model schools, provided teacher training, and carried out educational planning for the District Government.

Over 17,600 children in 123 government schools have directly benefited from improved school facilities and access to better education. This includes the children of football stitchers, who make up 20% of the rural population in the areas where these schools are situated. The programme also has a strong capacity building component: strengthening the education provided by local government and fostering the involvement of parents and rural communities.

*'I am working in this school as head teacher since 1988. I have got training regarding leadership role and school management, and pedagogical skills in Science, Mathematics, Urdu and English under Sudhaar-adidas quality education programme; with the extensive motivation Sudhaar developed and polished our attitudes towards education planning, resources*

*mobilisation and our teaching style as well. I have provided basic facilities to my school kid through the Sudhaar programme.* Ms. Zubaida Kousar, Head Teacher Govt. Girls Primary School, Mandair Kothay

**Ongoing - adidas America and football (soccer)**

adidas US works with football-affiliated organisations and athlete partners to promote access to football for disadvantaged, at-risk youth and kids. For example, our long-time athlete partner Eddie Pope, created his Foundation with the idea of using football to develop the mind, body and spirit of disadvantaged youth. The adidas Group makes financial and product contributions to help the foundation achieve its mission.

AmericaScores is a community-based, education organisation that uses football to teach urban children to apply the teamwork and responsibility they learn on the field to their work in the classroom. The adidas Group donates products in order to outfit all the children. Additionally, as part of a long-standing partnership with the US Youth Soccer Association, our financial and product contributions support TOPSoccer, a training and team placement programme designed to bring the opportunity of learning and playing football to youth with disabilities.

Those initiatives not only help to promote the football game itself, but help young people to develop their character and temperament.

Eddie Pope has been an adidas athlete partner since 1996, while the relationship with AmericaScore started in 1998 and with TOPSoccer in 1997.

**2006 - 'SOS Children's Villages', adidas Headquarters Germany and adidas South Africa**

'6 villages for 2006' was officially launched by SOS Children's Villages and FIFA in 2004, with the aim of raising funds to construct six new SOS Children's Villages. They will be built in Brazil, Mexico, Nigeria, South Africa, Ukraine and Vietnam. The campaign will run until the end of the final match of the 2006 FIFA World Cup in Germany. The adidas Group finances the construction of one family house of the SOS Children's Village in Rustenburg, South Africa.

HIV/AIDS presents a serious threat for the entire social and economic development in South Africa: 40% of all deaths between the ages of 15 and 49 can be traced back to AIDS. The number of orphans has risen astronomically in the past years due to AIDS and all local health authorities, relief organisations and politicians need to make a joint effort to get the catastrophic living situation of thousands of children under control.

SOS focuses on supporting children affected by HIV/AIDS through its Social Centres and Children's Villages. The adidas Group is helping to build the new SOS Children's Village in Rustenburg, in the north-west of the country. The city has 53,000 inhabitants and is located in one of the quickest growing regions of South Africa. However, speedy growth has its negative side: the number of people in need of help, and especially of children in need of help, is rising quickly.

In the SOS Children's Village in Rustenburg, children who are on their own and in need will receive family oriented, long-term care. This will give them the chance of a positive future and the opportunity to grow up with a sense of security.

## PERFORMANCE DATA

As part of our commitment to transparency, this section contains data about our performance during 2006. Most of the data included here is about our suppliers. It includes data on the size of our supply chain as well as the number of audits we conducted, and those conducted by independent monitors. Details of the training sessions we ran, and the extent of our Initial Assessments are also included. The environment data section covers management system certifications obtained by footwear suppliers, water and energy consumption as well as waste accumulation at our own sites, VOC levels in footwear factories and what freight method was used to ship our products. Key statistics about our employees and community affairs activities completes our presentation of data.

Performance data for 2005 can be found in the Performance data section of our website.

## Suppliers

### Number of suppliers per region and our own factories<sup>1</sup>

At May 1st, 2007, we worked with more than 1080 factories operated by independent business partners (excluding factories of our licensees). Supply chain consolidation remains a major part of our strategy to form strong partnerships with our suppliers. By placing larger orders more frequently with particular suppliers we can have a greater influence on their social compliance.

67% of our factories are located in Asia, 19% in the Americas and 14% in Europe and Africa. 22% of all these factories are in China.

Region	No. of Suppliers (excl. own factories)	No. of own factories	Total
Asia	723	2	725
Americas	193	8	201
Europe	153	3	156
<b>Total</b>	1069	13	1082

<sup>1</sup>Including Reebok but excluding licensee factories

### Number of supplier factories per country (May 2007)<sup>1</sup>

Country	Total number of factories
Argentina	10
Brazil	36
Canada	23
Chile	11
Colombia	4
Costa Rica	2
Dominican Republic	1
Ecuador	1
El Salvador	8
Guatemala	3
Honduras	10
Mexico	21
Peru	3
Uruguay	1
USA	67
<b>Total Americas</b>	201

Country	Total number of factories
Australia	11
Bangladesh	11
Cambodia	9
China	243
Hong Kong	7
India	48
Indonesia	56
Japan	56
Korea	75
Macao	1
Madagascar	1
Malaysia	14
New Zealand	5
Pakistan	7
Philippines	22
Singapore	4
Sri Lanka	21
Taiwan	40
Thailand	39
Vietnam	55
<b>Total Asia</b>	<b>725</b>

Country	Total number of factories
Albania	1
Bosnia & Herzegovina	1
Bulgaria	4
Czech Republik	1
Egypt	1
Estonia	1
Finland	1

France	3
Germany	4
Greece	8
Hungary	1
Israel	2
Italy	29
Latvia	1
Lithuania	1
Poland	2
Portugal	12
Romania	2
Russia	7
Slovakia	1
Slovenia	1
South Africa	18
Spain	14
Swaziland	1
Sweden	1
Switzerland	1
Tunisia	8
Turkey	26
Ukraine	2
United Kingdom	1
<b>Total Europe</b>	<b>156</b>

Total Asia	725
Total Americas	201
Total Europe	156
<b>Total Global</b>	<b>1082</b>

<sup>1</sup>Supplier production sites of the adidas Group (adidas, Reebok, TaylorMade), excluding licensee factories

**adidas Group licensees (May 2007)**

Product Range	Total no. of licensees	Total no. of factories producing for licensees	No. of countries where production is placed
Apparel	20	120	27
Hardware <sup>1</sup>	14	50	11
Footwear	3	5	1
Watches	2	7	1
Glasses	3	19	9
Cosmetics	1	4	4
Total	35 <sup>2</sup>	205 <sup>2</sup>	

<sup>1</sup> Accessories and gear

<sup>2</sup> 35 licensees source products from 205 factories in 37 different countries.

**Trainings in 2006 divided by region and type**

We aim to integrate supplier compliance into our core operations and build capacity in our supply chain. To achieve this we conducted 173 training sessions, including multiple group session trainings in adidas Group supplier factories, including licensee factories and factories of the Reebok business segment.

**Number of audits and trainings**

Year	2006 <sup>1</sup>	2005	2004	2003	2002
Audits <sup>2</sup>	1,101	916	954	906	1,148
Trainings	173	225	160	206	255

<sup>1</sup> Including audits and trainings in licensee factories and factories of the Reebok business segment

<sup>2</sup> Excluding FLA and other external audits; includes multiple visits in the same factory

**Type and Number of Training**

Region	General Compliance training <sup>1</sup>	Specific Labour/HSE training <sup>2</sup>	Environmental training <sup>3</sup>	Strategic Monitoring training <sup>4</sup>	Total trainings
Americas	24	3	1	3	31
Asia	48	31	0	27	106
Europe	21	3	1	11	36
Total Global	93	37	2	42	173

<sup>1</sup> General Compliance Training: E.g. Practical On-Site Training; Presentations for awareness raising

<sup>2</sup> Specific Labour/HSE Training: E.g. Worker-management communication; Sharing Best Practice; Freedom of Association; Factory Overtime System; Grievance & Appeal systems; Chemicals in production

<sup>3</sup> Environmental Training: E.g. Hazardous waste treatment; Environmental Best Practice

<sup>4</sup> Strategic Monitoring Training: E.g. Evaluation of compliance systems, administrators, and their efficiency

### Independent FLA Audits<sup>1</sup>

The FLA accredited the Reebok and adidas programmes in 2004 and 2005. As part of the 2006 obligations, adidas and Reebok received 43 independent, external monitoring and verification visits from FLA monitors.

FLA Year	Period	No. of audits <sup>2</sup>
1st	Aug 2001 - Dec 2002	42 Audits
2nd	Jan - Dec 2003	13 Audits
3rd	Jan - Dec 2004	12 Audits
4th	Jan - Dec 2005	7 regular FLA audits
		5 FLA audits as part of the FLA 'Soccer' project
		2 FLA factory visits as part of the adidas SOE programme assessment in 2005
5th	Jan - Dec 2006	43 Audits

<sup>1</sup> As part of the FLA membership

<sup>2</sup> From 2003 onwards, a new risk method was applied by the FLA, randomly selecting the factories to be independently audited. Hence the reduced number of factories subject to FLA audits.

### External Audits<sup>1</sup>

On behalf of the licensees, external monitors completed 24 audits in licensee factories. 25 external audits (not FLA and no licensee audits) were conducted on behalf of the adidas Group.

	Licensee audits <sup>2</sup>	External audits on behalf of the adidas Group
2004	60	2
2005	46	2
2006	24	25

<sup>1</sup> Excluding FLA audits

<sup>2</sup> Audits conducted in licensee factories by external monitors and internal licensee staff

### Number of warning letters issued to suppliers in 2006<sup>1</sup>

We issue warning letters when we see an ongoing serious lack of management commitment to improving compliance with our standards. In 2006, we issued a total of 11 warning letters.

Country	1st warning	2nd warning	3rd and final warning and recommended termination	Total warning letters
Cambodia	1	0	0	1
China	2	0	1	3
India	2	0	0	2
Indonesia	1	0	0	1
Philippines	0	1	0	1
Turkey	2	0	0	2
Vietnam	1	0	0	1
Total	9	1	1	11

<sup>1</sup> Excluding Reebok enforcement system

**Number of business relationship terminations due to compliance problems and rejections after Initial Assessment (IA) in 2006<sup>1</sup>**

We work closely with our suppliers to help them improve their performance. In situations of severe or repeat non-compliance we will terminate our business relationship with suppliers. In 2006 we terminated agreements with two suppliers.

We also work closely with Global Operations to pre-screen potential new suppliers. In total the SEA team conducted 144 Initial Assessments, with 117 accepted and 27 factories rejected, six less than in 2005.

Region / Country	No. of terminations per country	No. of rejections after PPA per country	Reasons for termination/rejection
<b>Asia</b>			
China		16	Poor management systems, falsified working hours and payroll records, coached workers, incorrect payment of wages and benefits, child labour, excessive working hours, no Sunday off, use of banned chemicals, poor house keeping, lack of fire and machinery safety, poor hygiene in kitchen and canteen, poor dormitory conditions
Indonesia		1	Incorrect payment of wages and benefits, insufficient social insurance, excessive working hours, use of banned chemicals, poor HSE conditions
Malaysia	1		Poor Labour and HSE conditions
Philippines		1	No management systems in place, no proper labour documentation available, poor labour and HSE conditions
Thailand	1		Lack of management commitment, poor Labour and HSE conditions
<b>Americas</b>			
El Salvador		1	Poor management systems, incorrect payment of wages and benefits, insufficient time recording system, use of banned chemicals
Honduras		1	Poor management systems, excessive working hours, no Sunday off, insufficient time recording system, insufficient social insurance
Mexico		1	Incorrect payment of wages and benefits, use of banned chemicals
<b>Europe</b>			
Turkey		4	Insufficient social insurance, incorrect payment of wages and benefits
Bulgaria		2	Incorrect payment of wages and benefits
Total	2	27	

<sup>1</sup> Excluding Reebok enforcement system

## Environment

### Environmental data for own production sites and main administration offices

Our own production sites	Energy consumption - Electricity (kWh/year)	Energy consumption - Heating Consumption (therms/year)	Water consumption (CUm <sup>3</sup> /year)	Waste (tons/year)
adidas Footwear Factory, Scheinfeld, Germany	1.557.038	141.433	1.668	248,20
adidas Apparel Factory, Suzhou, China	321.294	0	874	10,7
TaylorMade Assembly Factory, Carlsbad, USA <sup>1</sup>	4.185.372	13.995	376,9	72
Reebok-CCM Hockey Factory, Cowansville, Canada	2.730.400	37.323	861,93	446,91
Reebok-CCM Hockey Factory, St. Hyacinthe, Canada	2.241.000	47.565	9.892	39,36
Reebok-CCM Hockey Factory, St. Jean, Canada	2.979.000	104.570	7.773,64	153,36
Reebok-CCM Hockey Factory, Edmonston, Canada	1.387.800	0	1.789	95,24

Our main administration offices	Energy consumption - Electricity (kWh/year)	Energy consumption - Heating Consumption (therms/year)	Water consumption (CUm <sup>3</sup> /year)	Waste (tons/year)
Headquarters of the adidas Group, Herzogenaurach, Germany	11.635.564	298.639	22.199	567,61
adidas America Inc., Portland, USA	6.889.000	84.487	304,43	not reported
Reebok Headquarters, Canton, USA	15.073.743	464.908	350,77	764,37

<sup>1</sup> Figures cover TaylorMade Headquarters and assembly factory

**Certifications obtained by footwear supplier sites<sup>1</sup>**

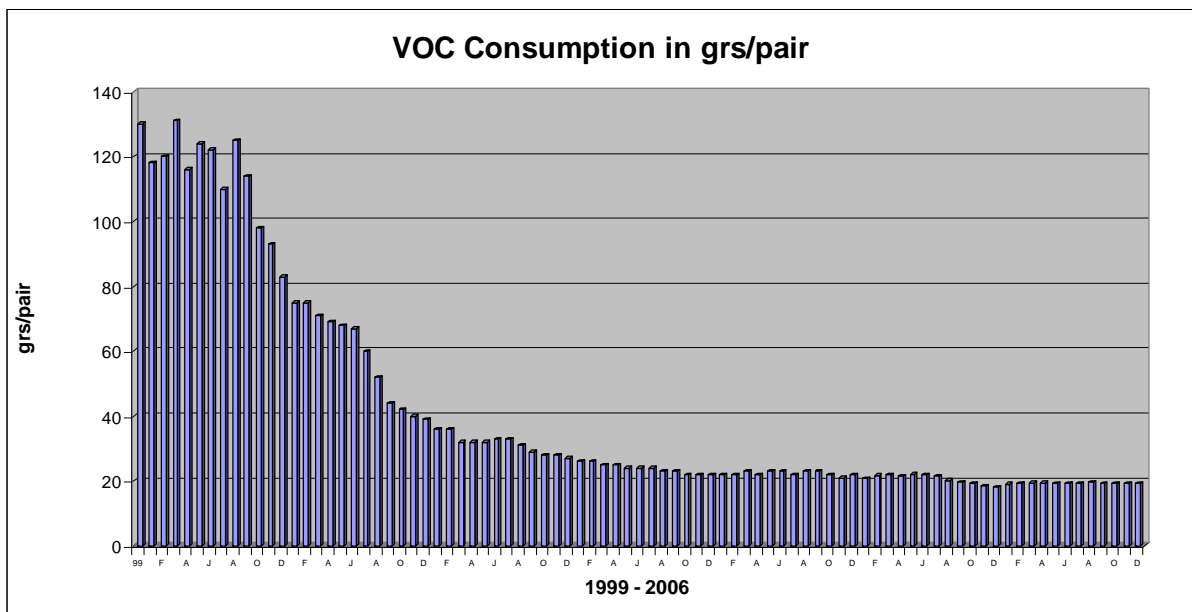
We encourage our suppliers to implement health, safety and environmental management systems as the best way to internalise a process of continuous improvement against our standards.

Country	Number of FW suppliers	ISO 14001	OHSAS 18001
Argentina	2	0	0
Brazil	3	0	0
China	11	10	10
Germany	1	1	1
India	1	1	0
Indonesia	6	4	4
Italy	1	0	0
Thailand	1	0	0
Vietnam	7	5	5

<sup>1</sup> Excluding factories from the Rockport business segment and licensee factories

**Reducing VOCs in footwear supplier factories**

VOCs are found in solvents used in the footwear manufacturing process. They can cause breathing difficulties and other health problems. Our target is to reduce VOC content to 20 grams/pair of shoes. The graph below shows the monthly average obtained from our footwear suppliers in China, Vietnam and Indonesia manufacturing more than 95% of our international footwear sourcing volume.



### Freight types used to ship adidas products<sup>1</sup>

Fuel used in transporting goods from where they are manufactured to the selling markets creates carbon dioxide emissions, which are a major contributor to global warming. We aim to minimise the environmental impact of transporting our goods by reducing our use of air freight, the form of transport that causes the greatest emissions of carbon dioxide.

% of products shipped	2006	2005	2004
<b>Apparel</b>			
Truck	21	22	22
Sea freight	72	73	69
Air freight	6	4	8
Sea and air freight	1	1	1

### Hardware<sup>2</sup>

Truck	3	4	4
Sea freight	95	95	91
Air freight	2	1	5
Sea and air freight	0	0	0

### Footwear

Truck	2	3	5
Sea freight	97	96	94
Air freight	1	1	1
Sea and air freight	0	0	0

<sup>1</sup> Figures expressed as a percentage of the total number of products transported

<sup>2</sup> Accessories and gear

## Employees

### Key Employee Statistics

At December 31, 2006, the Group's continued operations employed 26,376 people. This represents an increase of 66% versus the previous year's level of 15,935. This strong growth is mainly related to the acquisition of Reebok. In addition, new employees were primarily added in own-retail activities at brand adidas as well as adidas Asia. At the end of 2006, 48% of our total employees were women and 52% were men. Of the executive management positions, 25% were held by women and 75% were held by men.

Index/reporting unit		Total (Global)	adidas	TMaGolf	Reebok	HQ-Functions <sup>1</sup>
Total headcount (in %)	Male	52	52	68	52	44
	Female	48	48	32	48	56
Management positions held by (in %)	Male	75	71	87	77	80
	Female	25	29	13	23	20
Average age of employees (in years)		31.0	30.0	36.3	30.3	36.2
Employee-turnover (in %) <sup>2</sup>		10.9	10.3	15.5	12.7	6.7
Annual average length of service (in years)		5.5	4.0	5.0	8.4	6.6
Average number of training hours per employee/year		14.8	18.3	14.0	8.0	14.5

<sup>1</sup> Global Marketing, Global Operations, Global Corporate Services (e.g. Legal, Finance, HR)

<sup>2</sup> Voluntary attrition

**Health & Safety statistics for our own production sites and offices**

<b>Our own production sites</b>	<b>No. of employees</b>	<b>No. of workplace accidents</b>	<b>No. of lost days</b>
adidas Footwear Factory, Scheinfeld, Germany	65	1	4
adidas Apparel Factory, Suzhou, China	195	1	4
TaylorMade Assembly Factory, Carlsbad, USA <sup>1</sup>	850	8	38

<b>Our main administration offices</b>	<b>No. of employees</b>	<b>No. of workplace accidents</b>	<b>No. of lost days</b>
Headquarters of the adidas Group, Herzogenaurach, Germany	2282	7	not reported
adidas America Inc., Portland, USA	825	2	0
Reebok Headquarters, Canton, USA	1231	6	1

<sup>1</sup> Figures cover TaylorMade Headquarters and assembly factory

## Community Affairs

### Community projects and donations

In 2006, the adidas Group was involved in 1.379 community projects. The table below outlines the regions specific activities and the amount of our in-kind donations.

<b>Index/reporting unit</b>	<b>EMEA</b>	<b>Asia Pacific</b>	<b>Latin America</b>	<b>North America</b>	<b>Foundations<sup>1</sup></b>	<b>Total</b>
<b>Donation requests received</b>	<b>3.841</b>	<b>190</b>	<b>367</b>	<b>6.304</b>	<b>N/A</b>	<b>10.702</b>
No. of community involvement projects supported	25	12	1	13	1	53
No. of corporate giving activities	178	17	102	895	111	1.303
No. of employee involvement projects participated	3	8	1	11	0	23
<b>Total no. of community projects supported</b>	<b>206</b>	<b>37</b>	<b>105</b>	<b>919</b>	<b>112</b>	<b>1.379</b>
<b>Total no. of corporate volunteering hours</b>	<b>362</b>	<b>2.632</b>	<b>68</b>	<b>1.148</b>	<b>0</b>	<b>4.210</b>
<b>Total no. units of products donated</b>	<b>142.484</b>	<b>14.734</b>	<b>41.043</b>	<b>15.247</b>	<b>0</b>	<b>213.508</b>

<sup>1</sup> Adi Dassler Fund and Reebok Foundation

## REPORTING

We aim to act responsibly and communicate honestly. We recognise that stakeholders have a legitimate interest in our social and environmental performance and our ambition is always to satisfy that interest with complete and accurate information.

However, for 2006 we have not produced a social and environmental report that tracks progress and includes consolidated Group-wide data. We are however, updating this website so it reflects our current progress. Following the addition of Reebok to the adidas Group at the end of January 2006, we have built a Group-wide framework to generate reliable data about the newly combined supply chain and other corporate responsibility areas such as the environment or human resources. But consolidated data for 2006 does not exist.

Instead we produced a booklet that describes the steps we took in 2006 to create a unified approach to managing and measuring the new adidas Group's social and environmental impacts. One of those steps was to establish a central database for recording supplier performance, which will help us report in detail for 2007.

If you have anything to say about our reporting approach, we want to hear from you, so please do contact us and let us know what you think.

In this section you can find a chapter about awards and recognition and our position on verification of the data we report.

### Awards and recognition

We value feedback from our stakeholders about our programme and, of course we appreciate positive recognition from international institutions and rating agencies, non-governmental organisations (NGOs) and socially responsible investment (SRI) analysts. These organisations evaluate our work through in-depth analysis of the company's social and environmental programme, including document review and interviews with employees and management.

We have won awards and recognition from several organisations:

- Industry leader in the Dow Jones Sustainability Indexes
- Inclusion in the FTSE4Good Index
- Accreditation by the Fair Labor Association
- "Ökomanager" of the year 2005

- Best Sustainability Reporting for 2002 and 2004
- adidas Group among the 100 most sustainable corporations in the world
- Product rated best for quality and CSR by Stiftung Warentest
- adidas Group among Top Employers of the Year 2006

#### Industry Leader in the Dow Jones Sustainability Indexes

In 2006, adidas AG was included in the Dow Jones Sustainability Index for the seventh consecutive year. The index, which analyses the social, environmental and financial performance of more than 300 companies worldwide, rated the adidas Group as an industry leader on sustainability issues and CSR in the category 'footwear, clothing & accessories'.

#### **Inclusion in the FTSE4Good Index**

In September 2006, the adidas Group was again included in the FTSE4Good Index, which selects companies on the basis of ongoing commitment to environmental sustainability, strong financial performance, a positive relationship with stakeholders and dedication to upholding and supporting human rights.

This positive reassessment acknowledges the Group's social, environmental and ethical engagement, and encourages us to continue and intensify our efforts to improve our sustainability performance.

Set up in 2001 by the Financial Times and the London Stock Exchange, the FTSE4Good Index Series offers investors an insight into companies that fulfil the globally recognised guidelines for corporate responsibility. The indices are used by socially responsible investors around the world as a basis for structured products and index tracker funds.

#### **Accreditation by the Fair Labor Association**

In 1999, the adidas Group joined the Fair Labor Association (FLA), a non-profit multi-stakeholder coalition of private corporations, non-governmental organisations and universities. As a member, the company is subject to external monitoring by independent monitors, participation in the FLA third-party complaint system and public reporting.

Following an extensive review of the Group's compliance programme, the FLA accredited the monitoring programme of the adidas Group (which at the time did not include Reebok) in May 2005. Reebok had already become the first company to receive this FLA designation when its footwear compliance programme was accredited in April 2004. In June 2005, Reebok's apparel compliance programme was also accredited by the FLA. The programmes apply for re-accreditation every two years, and so Reebok's footwear compliance programme was re-accredited in October 2006 (by which time Reebok was part of the adidas Group).

The accreditation signifies satisfactory completion of a company's three-year initial implementation period and a finding by the FLA that the company is in substantial compliance with FLA requirements to implement a rigorous workplace code of conduct in factories making the company's products. In evaluating a company's programme for

accreditation, the FLA monitoring staff review independent factory monitoring and verification reports of supplier facilities conducted by accredited external monitors, and verify the implementation of monitoring protocols, training programmes and auditing systems.

#### **'Ökomanager' of the year 2005**

The World Wide Fund for Nature Germany (WWF) and German business magazine Capital named adidas Group's CEO Herbert Hainer 'Ökomanager des Jahres' (Environmental Manager of the Year). The jury valued the company's efforts in improving the ecological and social conditions in the factories producing its products.

#### **Best Sustainability Reporting for 2002 and 2004**

The German Chamber of Public Accountants awarded the 'Best sustainability reporting' prize to the adidas Group for its social and environmental reports 2002 and 2004. The jury especially emphasised the consistent high quality of the sustainability reports and the proactive management of specific issues.

#### **adidas Group among the 100 most sustainable corporations in the world**

In 2007, the adidas Group was included for the third consecutive time in the list of the **The Global 100 Most Sustainable Corporations in the World**. The Global 100, a selected group of companies taken from a pool of some 1,800 international companies, provides investors and other stakeholders with a unique evaluation tool. Launched in 2005, the annual Global 100 is announced each year at the World Economic Forum in Davos.

#### **Product rated best for quality and CSR by Stiftung Warentest**

Before the start of the 2006 FIFA World Cup™ in Germany the adidas +Teamgeist match ball obtained the **best** rating of all ball products tested by the German consumer group magazine Stiftung Warentest. Our +Teamgeist match ball was chosen not only for its functionality, quality and material safety but also for the suppliers' working conditions and the overall CSR (Corporate Social Responsibility) performance of the adidas Group.

Stiftung Warentest has been assessing the social and environmental performance of companies in product manufacturing since 2004. During the evaluation process we provided detailed CSR information about the Group's social and

environmental programmes and initiatives, the products and the supplier sites. Part of the rating approach was the external validation and verification of information we submitted. Verification audits were conducted at the two supplier sites in Thailand and Pakistan, following a verification visit at our Headquarters in Herzogenaurach, Germany.

**adidas Group among Top Employers of the Year 2006**

adidas AG has been voted as one of the Top Employers in Germany by 'karriere' magazine. The overall ranking, which was conducted by the Corporate Research Foundation, lists adidas AG as number six in the list of Top Employers in Germany. In the category 'Job Security', adidas AG comes in a close second. In the category 'Market Leader' adidas ranks third.

Also in 2006, we ranked second in a list of the 100 most attractive employers for business students according to The European Student Barometer, the largest survey of university students across fourteen European countries conducted by the trendence Institute for personnel marketing.

**Statement on verification**

We recognise that some stakeholders want companies to ensure the content and data disclosed in their sustainability reports is independently verified. While we strive to continuously improve our reporting systems for supplier monitoring data, we feel that much of this data, in particular data on labour conditions, is not always verifiable in a standardised way. At this stage therefore we do not feel that a report verification would add value. We do, however, believe that independent verification of workplace conditions and of the processes and monitoring approaches we adopt in our compliance programme is important. For this reason the report does contain information that is subjected to an annual review by the Fair Labor Association. We also refer to data verified when supplier factories or our own facilities were certified to ISO, EMAS and OSHAS standards.

See also our Statement on disclosure and transparency of factory data in the Statements section of our website.

## CONTACT

We welcome your views about our efforts to become a more sustainable company. You can contact us at:

adidas AG  
Social & Environmental Affairs  
World of Sports  
Adi-Dassler-Straße 1  
91074 Herzogenaurach  
Germany

Phone: +49 (0) 9132 / 84 – 0  
Fax: +49 (0) 9132 / 84 – 3242

**For inquiries to our Social and Environmental Programme please send a mail to [sustainability@adidas-Group.com](mailto:sustainability@adidas-Group.com)**

**For media inquiries please send a mail to [corporate.press@adidas-Group.com](mailto:corporate.press@adidas-Group.com)**

## Complaints

We want to know if anyone has complaints about conditions in our suppliers' factories.

If you have a complaint to make, you can contact us with the specific details of the case and we commit to taking your complaint seriously.

We appreciate that you may want to contact us anonymously. This does not change the seriousness we give your complaint although it does affect the process we follow:

1. We investigate **all** complaints we receive.
2. We will reply to you requesting further contact to establish the full details of your complaint. However, we understand if you wish to remain anonymous and do not wish to identify yourself.

3. We speak to all the other parties involved to establish the full facts of the matter and determine if our supplier has a case to answer.

4. If so, we inform the supplier and specify remedial action for the supplier to take in order to address the issue.

5. Unless your complaint was anonymous, we will contact you to inform you of the results of our investigation and the steps we are taking.

### *Independent complaints process*

We understand if you do not wish to complain to us about one of our suppliers. If this is the case, there is an independent process available to you through the Fair Labor Association, of which we are a member.