FINANCIAL RESULTS PRESENTATION

First Quarter 2009 Speech

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John-Paul O'Meara, Head of Investor Relations

Good afternoon ladies and gentlemen and welcome to our first quarter 2009 financial results conference call. I'm JP O'Meara and I head up the IR activities here at the adidas Group.

Our presenters today are Herbert Hainer, adidas Group CEO and Chairman, and Robin Stalker, Group CFO. Today, they will be covering the Group's first quarter financial performance, but more importantly, spending some time introducing you to several new initiatives, which will create a new platform to drive our business forward over the next few years.

Herbert Hainer, CEO and Chairman

Thanks JP and good afternoon ladies and gentlemen.

You just have to read the papers today to see the significant burden the economic climate is having on corporate profitability and we have to accept that this is an unavoidable consequence of the downturn. For the adidas Group, our success in 2008 certainly hasn't made life any easier in these challenging times. We not only profited from the UEFA EURO 2008™ and the

Beijing 2008 Olympic Games, but also from buoyant emerging markets. All these factors make comparisons with last year's first quarter extremely hard and are reflected in our results.

- Group sales came in at 2.6 billion euro – down 2% – or a 6% decline in currency-neutral terms.
- Gross margin decreased 400 basis points to 45.2%.
- And diluted earnings per share were 4 cents compared to a record 79 cents a year ago.

While our bottom-line development is clearly not satisfactory, fundamentally the profitability of our business is solid and you will see this improve considerably as we work our way through the year. I'll let Robin go through the specifics related to a significant amount of one-offs we had in the first quarter – but before that let me take a few minutes to walk you through where we are with our brands and what the underlying trends in our key markets are.

When it comes to our top-line performance, I believe our brands have done reasonably well in the first few months of this year as we continue to win over consumers with the concept and product firepower which is at the heart of our organisation.

- At brand adidas, we continue to connect with more and more consumers, highlighted by double-digit sales increases in the Sport Style division.

- At Reebok, we are making solid progress on rebuilding our connection to the female consumer with the women's segment up at double-digit rates during the quarter, driven by recent launches in fitness and walking.

- And at TaylorMade-adidas Golf, our market share has increased significantly in several categories including metalwoods and irons.

Let's look briefly at each brand in a bit more detail.

adidas is a powerful brand built on a rich heritage and passion for the impossible. And even despite the crisis, the amazing bond this brand has with consumers around the world continues to grow. Although sales were down 6% currency-neutral in the first quarter, we have certainly strengthened our position in several markets and categories around the world. Some of the highlights include:

- Our performance-enhancing TECHFIT™ apparel, which is growing strongly.
- In outdoor we had double-digit increases in a category we are putting more and more resources behind.
- In basketball we are making big strides in Asia, where in markets like China, this sport is the most viewed and most played.

- And in running we had a stable development globally, with big performances from our Supernova and adiStar product families.

However, our biggest step forward this quarter at brand adidas has been in the Sport Style division. Sales are up 12% currency-neutral. In an economic downturn, the lifestyle segment can be more exposed as the consumer tends to be more selective. This result therefore underpins just how desirable the adidas brand is today to the young trendy consumer. I’m sure you’ve all seen our eye-catching House Party campaign – the biggest brand campaign in the history of Originals. And we will continue to energise this space throughout the rest of the year as we celebrate our 60th birthday under the banner of “60 Years of Soles and Stripes”, and through unique collections like Originals by Originals and the extension of new lines such as Style Essentials.

At Reebok, we are still away from the financial performance we had expected to be delivering now three years after the acquisition. The last years have been tough. The damage that had been done to the brand after years of careless distribution was higher than we expected. And this is still impacting our profitability development today.

However that being said, I have never doubted the potential of the Reebok brand. Our refined brand strategy to Own Women’s Fitness, Challenge Men’s Sport and Revive Classics is really starting to kick in. We’ve had a lot on the drawing board, and now we are seeing that with consistency of approach we can indeed turn our ideas into commercial success. For the first quarter, segment sales increased 1% in euros, and declined 4% on a currency-neutral basis in line with our expectations.

Let’s look at our Women’s initiatives. Reebok’s partnership with Cirque du Soleil was brought to life in February with the launch of JUKARI Fit to Fly™, a new workout experience especially designed for women. The response has been nothing short of phenomenal, with outstanding media coverage generating high consumer interest. In LA, our mobile JUKARI Celeb studio was the talk of the town with the likes of Brooke Burke, Mischa Barton, Regina King and a host of others taking to the FlySet™.

Another key product initiative, the EasyTone™, which helps tone key leg muscles, has been a hit at retail, selling through at rates as high as 20%, and is one of the top-selling shoes at Lady Foot Locker. With a price point above $100 this kind of result is exceptional in the current economic climate when consumers are tending to trade down. Both these concepts are leading to commercial success with sales in the women’s segment up at double-digit rates in the quarter.

Innovations like these – whether concepts or products – are our most important tools for rebuilding the connection to the consumer and getting Reebok back onto retailers’ shelves. We are creating a lot of positive energy right now with customers and consumers alike. In markets like Germany, Scandinavia, Japan and India, we are harnessing elements from all three pillars of our brand strategy, driving positive momentum.

Turning to TaylorMade-adidas Golf, the golf industry is off to a very weak start in 2009, with most major markets around the world contracting at double-digit rates. Nevertheless, TaylorMade-adidas Golf continues to significantly outperform its competitors with sales down only 6% on a currency-neutral basis, including the consolidation of Ashworth. In Europe, revenues increased 11% currency-neutral and that's on top of a 48% increase in the first quarter last year. Our recipe for success at TaylorMade is threefold: 1) having the right product, 2) building early demand and 3) launching at the right time. And we executed flawlessly in the first quarter.

The launch of our R9™ driver in March is a great example of this and contributed to TaylorMade’s strongest ever March sales in its history in the US. The R9™ is already the top-selling driver at retail in the US and is the number one played driver on the major worldwide golf tours. We also set a new market share record for TaylorMade in irons, adding four percentage points during the quarter due to the success of our Burner 09 line. Now entering the important golf playing months of the year, we continue to follow this formula. And I fully expect that we will stay on top of the leaderboard. Take last Sunday for example, where TaylorMade-adidas Golf Tour Staff professional Sean O'Hair won the Quail Hollow Championship in Charlotte, North Carolina, one of the premier events on the PGA Tour, and his first tournament win of the year. He was head-to-toe in our brands, using TaylorMade's new R9 driver and TP Red LDP ball, wearing adidas shoes and Ashworth apparel.

So as you can see, all of our brands are making good ground with our key concept and product initiatives for 2009. However it is clear we have had varying results by region and country. Let me quickly take you around some of our key markets to tell you how we see things from today's standpoint.

First of all the emerging markets. If I exclude Russia and China which I will come to separately, sales in the other emerging markets were up 16% in the first quarter, maintaining the same pace as in the prior year. Latin America in particular is very solid, and I expect these markets to outperform all other regions this year.

Turning to Russia, fundamentally the market continues to be healthy, although growth has slowed considerably versus prior year levels. Our volumes continue to increase for both adidas and Reebok. We have strengthened our market leadership position adding to our store base, which for the Group is now in excess of 750 own stores. However, the development of the Russian rouble has been a major factor in our profitability this quarter and accounts for about one-third of our total Group gross margin decline. We are working on combating this through price increases, and also from an operating cost point of view we are reviewing our rent terms wherever possible. However, both these steps will still take a while to turn the profitability impact around.

In China, the market still has a few short-term challenges to overcome. Inventories in the channel are still too high as a result of oversupply by several brands in 2008, and as a consequence sales for the Group declined in the first quarter. For adidas and Reebok the story however is quite different. With adidas we are the premium sports brand in the market, and intend to nurture this position for the long term. That means taking a very disciplined approach towards supplying the market and, for the sake of a quarter or two, I believe this is in the best interest of the brand. Nevertheless, I expect our profitability in China will remain very solid even as we continue to invest in this important market for the long term. We have scaled back our expansion plans to focus on new or under represented store formats like Style Essentials, Originals and factory outlets.

For Reebok, we have taken a different approach. As we simply grew too quickly in China, we are rationalising our store base to remove unproductive stores and poor locations. To achieve this as rapidly and painlessly as possible, we have incentivised our retail partners in the first quarter. Although this led to a significant impact on sales and gross margins, we believe this is the right thing to do at this stage of Reebok’s development in China.

And to wrap up, let me briefly comment on North America, where we have taken somewhat similar steps. As we told you in March, this market would be our most challenging in 2009. There is still a lot of nervousness at retail as comp store sales are poor, and there is still a lot of uncertainty towards the prospects for the all-important back-to-school season.

For adidas – to ensure our offering stayed fresh and positioned correctly – we proactively took back product early in the year to channel it through our factory outlets. This action accounted for more than one-third of the brand's sales decline in the first quarter but did lead to an increase in our retail margins during the period. The majority of this action is behind us now and we expect to be in a significantly better position at the end of the second quarter. I have no doubt it was the right thing to do in the interest of our cornerstone brand.

At Reebok, our sales also declined significantly due to the environment but also as a result of our decision to exit the $29.99 price point. Here I do have some good news to share. At this time last year, over 35% of our offering in the US was at that price point. Today the figure is below 10% and we are completely clean at all our key strategic accounts.

So on that note ladies and gentlemen, as I told you in March, there is no doubt that the consumer is spending less in 2009. While at a first glance our results appear disappointing, I believe on a deeper look and being mindful of all that is going on around us, the adidas Group has shown a lot of resilience. And, more importantly, we have been disciplined and consistent with our long-term strategies.

I'll be back in a few minutes to tell you more about our cost savings plan which will also see us significantly change the shape of our organisation. But first, Robin will take you through the rest of the financials.

Robin Stalker, CFO

Thank you, Herbert, And good afternoon ladies and gentlemen.

As Herbert has already given you a flavour of our main achievements and also the detail on some of our key markets, I would now like to provide you with some more colour on our financial results and the numerous one-time effects that played a role below the top line. I'll also put particular emphasis on giving you a feeling for our expectations for the remainder of the year.

So let me quickly recap on our top-line development where currency-neutral sales declined 6%, or 2% in euros to 2.6 billion euro. Currency translation effects had a significant impact on sales in several markets – some extremely negative like in Russia and the UK, but also some positive such as markets closely tied to the US dollar, and of course Japan.

With the exception of Latin America, where currency-neutral sales increased 31%, revenues declined in all regions. In Europe, sales were down 5%, in Asia sales declined 6%, while in North America revenues declined 17%.

While we are clearly disappointed with our development in North America as Herbert has already mentioned, don't forget we also ran up against exceptionally high comps from the prior year, in both

- Europe, where we benefited from the UEFA EURO 2008™,

- and Asia, where we showed 60%-plus sales increases in China in the lead-up to the Olympic Games.

Turning now to the other P&L items, you clearly saw the effect higher input costs, currency devaluation and the more promotional retail environment had on our Group's gross margin. It was down 400 basis points to 45.2% in the quarter (versus 49.1% in 2008), with declines in all of our brand segments. As a result, Group gross profit for Q1 decreased 10% to 1.2 billion euro.

There were three major factors impacting this performance.

- First, almost half of the overall decrease for the Group relates to higher sourcing costs which we have discussed in detail last year. Here, although we expect the pressure to lessen in the second half, the easing of input prices will not play a positive role until 2010.

- Second, one third of the overall decrease in gross margin is a result of currency devaluation effects – largely related to the Russian rouble which has depreciated significantly over the last couple of months. As we have told you before, due to the fact that we cannot cost-effectively hedge the rouble, this squeezes gross margin as our cost base in Russia is largely US dollar denominated.

- And finally, a highly promotional retail environment and higher clearance activities accounted for the balance of the decline.

While these factors were relevant for all of our brands in the quarter, their weighting in importance differed.

- At adidas, higher input costs and the Russian rouble accounted for nearly all of the decrease.
- In the Reebok segment, one-third of the decrease was due to higher sourcing costs, around one-third a result of the promotional environment in the US and China, and the remainder due to the Russian rouble and lower margins due to the first-time inclusion of our new companies in Latin America.
- Finally, at TaylorMade-adidas Golf, two-thirds of the decrease was due to price repositioning and product mix as a result of the difficult golf market, with the remainder due to the consolidation of Ashworth where we had a 2 million euro non cash charge for purchase price allocation.

Moving below the gross profit line, other operating expenses as a percentage of sales increased 470 basis points to 44.7%. This development reflects the large number of own-retail stores we opened throughout 2008 and the resulting additional costs compared to the first quarter of last year. Marketing working budget did not play a major role as we balanced additional expenses for highlight brand initiatives such as the House Party campaign at adidas and the introduction of “JUKARI Fit to Fly™” at Reebok with savings in other areas and categories.

The biggest deviation in our operating expenses compared to the prior year however was due to items that I consider one-off in nature. So let me spend a few words on each of them.

- Firstly, given the difficult retail environment and in line with our conservative accounting policies, we felt it prudent to increase our allowance for doubtful debts by 34 million euro.

- Second, as we announced in March, we carried out some restructuring measures at Reebok and its related operations such as headcount reductions in the US and the UK, the closure of our UK office in Bolton, and also, expenses to prepare the organisation for the introduction of a joint adidas and Reebok operating model in Europe and Latin America. This resulted in restructuring charges of 26 million euro, of which 21 million euro were recorded in the Reebok segment and the remainder in HQ related to the Reebok sourcing function.

- Third, the integration of Ashworth into the TaylorMade-adidas Golf segment led to one-time effects of 5 million euro for the segment. To complete the integration, which largely involves winding down non core operations, we will incur further charges of around 25 million euro through the remainder of the year, around half of which will be in the second quarter.

- Fourth, the disposed Gekko business, which we acquired as part of Ashworth and divested in the first quarter, had a negative 9 million euro impact on operating profit in the HQ/Consolidation segment where it was reported under assets-held-for-sale at year-end.

- And finally, to complete the comparison with the prior year, we had a 6 million euro gain in the first quarter of 2008 for the divestiture of the Maxfli brand to Dicks Sporting Goods.

Taken together, this gives you a total of 80 million euro in restructuring and other expenses that I consider one-time which negatively impacted operating profit in the first quarter.

To wrap up my discussion on operating profit, Group royalty and commission income in the quarter decreased 4% to 20 million euro. The replacement of distributor agreements in Latin America with new Reebok companies was the main driver behind the decline.

All in all, these factors led to an operating profit decline of 79% to 58 million euro from 282 million euro in the prior year and an 8.5 percentage point operating margin decrease to 2.2%.

Moving over to the non-operating items of the P&L, net financial expenses increased 56% to 49 million euro during the first quarter of 2009. Due to a lower average interest rate on gross borrowings, interest expenses remained virtually stable compared to the prior year despite the higher level of net borrowings. As in the fourth quarter, however, we took a hit from the revaluation of subsidiary balance sheet positions denominated in foreign currencies that have weakened against the respective functional currencies. This quarter, the effect amounted to 19 million euro. Let me emphasise again that this is purely a result of the unprecedented exchange rate volatility we are seeing at the moment.

This development coupled with the decline of operating profit led to a 97% decrease of both IBT and net income attributable to shareholders. A sharp increase of the Group's tax rate negatively impacted the latter. While we should not overemphasise the tax rate development due to the low absolute level of IBT, we remain cautious with regard to the full year tax rate. Adverse shifts in the regional mix of our earnings as well as the non-recurrence of prior year one-time tax benefits will most likely lead to an increase of the Group's tax rate versus the prior year level of 28.8%. Finally, basic and diluted earnings per share decreased 97% and 95%, respectively, to 2 and 4 cents.

As a result of our first quarter performance, and our expectations for the remainder of the year, we are now in a position to give you some more colour on our earnings per share guidance for the full year. As the environment hasn't eased and many of the factors I have outlined in my discussion will persist in the second quarter, we expect to breakeven in the first six months of 2009, with a strengthening of profitability in the second half of the year, albeit at lower levels compared to the prior year.

Let’s turn to the balance sheet. Working capital management was already a challenge in the fourth quarter and – as we expected – this did not substantially change in the first quarter. In Q1, inventories grew 18% in currency-neutral terms or 28% in euros to slightly above 2 billion euro. While this is certainly higher than we would have liked, growth moderated compared to the fourth quarter. Nevertheless, it is clear that we placed production orders for the first half of 2009 at a time when we had higher sales expectations. Rest assured we have markedly reduced sourcing volumes for the second half of the year, and have tight controls in place so that we will return to more normal levels of inventory towards the end of the year.

Accounts receivable were up 11% on a currency-neutral basis and 15% in euro terms, to 1.9 billion euro. The increase was broad-based across all brands and regions. While the level of payment defaults remained similar to prior years, we have nonetheless taken a higher allowance for doubtful accounts as I have already mentioned, to account for the challenging macro environment and the financial constraints many of our retail partners are facing today.

As a result, average operating working capital came in at 25.6% – an increase of 90 basis points from 24.7% in the prior year.

Obviously, the development I just described also affected our debt situation. At the end of March, net borrowings amounted to almost 2.9 billion euro, an increase of 39% (or 810 million euro) versus last year. Also here, currency movements played a negative role, accounting for 136 million euro of the increase. And, last year's share buyback distorts comparisons of the underlying development by 275 million euro. As a consequence, financial leverage at the end of the first quarter was 81.8% – an increase of 9 percentage points compared to the prior year level.

Let me emphasise that reducing net borrowings remains one of the key priorities for our Group in 2009. We are committed to making progress towards our medium-term financial leverage target of below 50%. We are exerting high discipline in investment activities. We do not plan another share buyback for the time being. And we expect continued strong cash flows from operating activities to support achievement of that goal.

Now back to Herbert who will give you more detail on our outlook for the rest of 2009...

Herbert Hainer, CEO and Chairman

So moving on, I want to update you and share some very significant details about the measures we are taking to ensure the adidas Group not only deals with the challenges of today's marketplace, but also to position our company for the long term.

When it comes to cost, there are no “sacred cows” here at adidas Group – everything is on the table. However, we recognise – and so should you – that we are a premium-branded global company. And we need to balance our desire to right-size the business with our need to keep our brands strong and invest when necessary, so we do not take liberties that would damage long-term health.

Nevertheless, as with all growth companies, there is still fat acquired through rapid expansion and ways we can improve our structures and processes. And we are a company that has gone through rapid expansion and also through rapid transformation. Since 2000, the adidas Group has grown significantly in complexity from 95 companies to 190 represented in all regions of the world. During that period our business has also transformed from predominantly wholesale to include a far more significant retail component. With over 1.8 billion euro in own-retail sales in 2008, we are on a growth path that will make us one of the top 250 global retailers in the medium term.

As you will have seen in today’s results and our other announcement this morning, we are already well under way with our plans to address these issues. This is a result of several months of intensive examination through which my Board colleagues and I have set the necessary action plans into motion.

These are broadly broken down into four major buckets.

- Firstly is rightsizing and further integrating our business units. A lot of this has already taken place in the first quarter through headcount reductions of over 500 at Reebok, Rockport and TaylorMade-adidas Golf, as well as the joint operating model we set up in Europe and Latin America. This represents about one-third of our planned savings, with most of the costs already taken in the first quarter.

- Second, as we have just announced this morning is the implementation of new Group-wide global wholesale and retail structures. For wholesale this is a necessary change. As more and more of our key accounts spread their wings globally through this structure we can harness the significant leverage of our size more effectively. But more importantly, at this time we need to implement a dedicated unit of retail professionals to support our growing own-retail business, which is an integral part of the Group's controlled space strategy. Under the new leadership of Michael Stanier who joins us from Gap in June this year, we will place a high focus on increasing the efficiency of our retail operations with a particular emphasis on improving our store productivity, and aggressively eliminating unproductive stores.

- Third, which we have also just announced this morning is the reorganisation of our operating structures to eliminate an entire layer of our organisation – the regional headquarter. This means that, going forward, the Group will no longer operate regional headquarters in Europe and Asia. Instead, it will strengthen the direct interaction between the global organisation and the local markets. This new set-up will significantly increase speed-to-market.

- And finally, the streamlining of our sourcing and product creation processes and organisation to improve efficiencies and ensure we are focusing on those opportunities that provide the biggest potential.

All Group functions such as Operations, Finance, HR, Legal and IT will also undergo changes to reflect the new organisational structure while identifying shared service opportunities to drive further efficiencies.

Through the initiatives I have just outlined, it is our goal to generate in excess of 100 million euro in annual cost savings upon the various project completions, and I expect we will have all these measures in place by the end of 2009. Costs to achieve this goal should roughly equal one year’s savings.

But this is not all we will be busy on during the coming months. Our brands will continue to keep the finger on the pulse with the consumer. At adidas – this summer – we will start our build-up for next year’s Football World Cup with the FIFA Confederations Cup in South Africa. At Reebok, we will expand on our women’s initiatives with new variations to the product assortment and completing the global launch of EasyTone™ on July 1. Reebok will also be bringing out the next in our series of running shoes featuring the KFS technology, and launching a new campaign called “Born from Sport” supporting the revival of our Classics business. And at TaylorMade-adidas

Golf, we will be extending our new R9™ family of drivers as well as entering a key volume market in footwear with the expansion of the FitRX at a price point of $99 launched a few weeks ago.

So to sum things up for today, I know that our results for the first quarter may not appear satisfactory. But I also think you can see that we are not resting on our laurels and just waiting for the crisis to end. We are attacking it head on, working on many initiatives to strengthen our organisation for long-term success.

At the same time, we will manage our brands in a controlled and consistent way, ensuring our inventories and distribution channels are clean, enabling us improve our market positions and increase our market share in a profitable and sustainable way. And this will be reflected in our numbers as we go through the year.