

staying focused

social and
environmental
report 2003



adidas-Salomon

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Staying focused /// As any athlete knows, to achieve your aims you must stay focused – whatever the pressures, however difficult the conditions. It's the same for adidas-Salomon. To achieve our aim of developing as a socially responsible business, we maintain our focus through a process of continual improvement. We use our creative and competitive drive to reach for new goals... we respond to our stakeholders, and to the challenging environments we operate in... finally, we review our performance against targets, using this information to set ourselves new goals. And so the cycle begins again.

Through this holistic approach, we will continue to meet the challenges we face and drive forward our corporate social responsibility programme.

BUSINESS CHALLENGES ///

Like any global business, adidas-Salomon must manage wide-ranging commercial and competitive pressures to deliver growth. At the same time, we have a responsibility to ensure decent working conditions and environmental standards throughout our global supply chain.

Our business and the world we operate in, impact on our Corporate Social Responsibility (CSR) activities in subtle and sometimes unpredictable ways.

In 2003, for example, the SARS epidemic and increased acts of terrorism curtailed our ability to implement some Standards of Engagement (SOE) compliance activities, while globalisation and corporate scandals contributed to increased demands for transparency and reporting. Within the business, training and capacity building exercises revealed wide variation in compliance awareness across the supply chain.

Below we summarise our key business challenges.

GLOBAL TRENDS /// Trends are developing that will put extra pressure on our SOE - our code of conduct for business partners. Production sites for apparel will be located in closer proximity to material production, causing different dynamics for influencing compliance in the supply chain; multi-tiered supply chains, which manage production processes for raw materials to finished product, are proliferating; and manufacturers themselves are becoming multinational, with subsidiary sites in emerging global markets.

Perhaps the most significant change will be the end of the Multi Fibre Agreement (MFA) on December 31, 2004. Through the MFA, quotas were set limiting exports of clothing and textiles from developing to industrial countries. Although designed to protect the industry in the developed world, developing countries have come to depend on quota allocations to drive the growth of their textile and garments industries.

With the end of quotas, countries outside the original MFA group will be able to trade freely, at lower cost - which makes the future of the clothing and textile industry in some developing countries uncertain. Additional trade restrictions, anti-dumping measures and bilateral agreements may also come into force.

Our response to this complex situation is to complete the consolidation of our garment sourcing around six strategic countries (China, India, Indonesia, Thailand, Turkey and Vietnam), supporting these with smaller operations in Central

America, Cambodia and the Philippines. This strategy not only offers the Group flexibility and security in the supply of apparel products, but also reinforces our longstanding relationships with key suppliers.

MANUFACTURING ISSUES ///

Improving supply chain efficiency Manufacturing at optimum efficiency is a business imperative but can have a harmful effect on supply-side wages and employment levels. In 2003, production efficiency measures introduced into some supplier factories reduced the need for overtime, which in turn reduced total take home pay; other factories experienced redundancy and lower employment levels. In other cases, however, greater efficiency resulted in higher wages, and stable or increased employment. The impact of these programmes depends on the way in which they are implemented by management.

Similarly, in the drive to reduce product inventory and meet tighter delivery deadlines, it is important to have sound human resource, health and safety and environmental systems in place, to help manage change in the workplace and ensure that compliance is not compromised.

Ensuring a fair wage A pilot study of fair wages in Indonesia found that achieving a fair wage is not just a matter of identifying a formula; it has to be underpinned by transparent wage negotiation processes with worker participation, and effective human resource and production efficiency programmes.

Consumer satisfaction Consumers naturally want the best quality product at the best price. We balance this with our suppliers' responsibility for the welfare of their employees. In 2003 we assessed our suppliers' performance against a wider range of SOE and manufacturing benchmarks. Not all suppliers could deliver against all these parameters, which resulted in some existing relationships being terminated, and the intake of new suppliers reduced.

Consumers also expect high performance from our products, which makes our component materials and manufacturing processes increasingly complex. To address this issue in 2003 we focused on production floor ergonomics and increased collaboration between the Social and Environmental Affairs (SEA) and Lean Manufacturing teams.

ABOUT THIS REPORT /// This report describes the social and environmental performance of the adidas-Salomon Group during 2003. The report sets out our goals, strategy and actions in improving working conditions in our suppliers' factories and lessening our environmental impact. It refers back to the objectives and targets given in last year's report, and assesses our progress in meeting them. It highlights social and environmental aspects identified as significant by our stakeholders, and describes targets for the next reporting period. The report has been released at the same time as the annual financial report to give stakeholders a complete picture of our business.

GLOBAL REPORTING INITIATIVE GUIDELINES /// To help us meet globally accepted standards of content, each year we move closer to the Global Reporting Initiative's (GRI) Sustainability Reporting Guidelines. The index on page 50 enables the reader to check the content of this report against GRI guidelines and identify where there are gaps.

AVAILABILITY /// The Social and Environmental Report is available in English and German language versions. This and previous years' reports and further information can be found on our website, www.adidas-salomon.com/en/sustainability/. Contact details are on page 52 of the report, as well as on the website.

CEO STATEMENT /// Last year's Social and Environmental Report highlighted the importance of earning the trust of stakeholders. Throughout 2003 we have aimed to achieve this through open dialogue, and by acting responsibly and communicating honestly. These are not just actions to fulfil a communications agenda, but are part of who we are – our values as a brand – and what we are striving to become: a global leader in the sporting goods industry.

Being an industry leader means more than delivering strong financial results. While that is important, what is equally important is how we achieve that success. Good governance, managing our environmental impacts and improving working conditions in our suppliers' factories are all central to our view of business leadership. Stakeholders, including our own employees, expect us to do more across all these areas, which drives us to ever higher levels of performance.

Continuous improvement demands a systematic approach and clear targets. But to achieve success, athletes need to do more than set standards for their own performance. They must adapt to the conditions they encounter on the field of competition. Likewise at adidas-Salomon we have defined our Standards of Engagement, but to achieve our ultimate goal we need to respond flexibly to feedback and to the local conditions we find in the countries where our suppliers operate.

In this, our fourth Social and Environmental Report, we record our achievements against our 2003 social and environmental targets and publish our targets for 2004.

A key achievement in 2003 was extending our Standards of Engagement programme to licensees and brands in the adidas-Salomon Group not previously covered. Rather than simply police compliance with our standards, we continued to facilitate improved performance. We still audit our suppliers, but instead of highlighting non-compliances, we focus on addressing the reasons for non-compliance. To support this

shift in emphasis, the supplier training programme has grown substantially during the year. Despite the significant disruptions to travel plans caused by SARS, we facilitated more than 200 training sessions in 2003, twice the year's target. The training sessions themselves are also increasingly tailored to relevant country risk and supplier compliance performance, such as environmental best practice and worker-management communications.

Listening closely to stakeholders helps us develop our programme. In response to earlier stakeholder feedback, in 2003 we engaged workers in dialogues, exceeded the number of independent audits required by the Fair Labour Association (FLA) and shared our fair wage study more widely.

Benchmarking our last report against the GRI guidelines has helped us move closer to meeting the GRI requirements. This report includes a gap analysis that highlights those areas where we are fulfilling the guidelines and where we are not. Such efforts to act responsibly and report transparently have not gone unnoticed. For the fourth year in a row the Dow Jones Sustainability Index has listed adidas-Salomon as a leader in our industry. We are also included in the FTSE4GOOD Europe Index and on Ethibel's ESI Europe Index.

Despite these successes, we have not achieved everything we set out to do. The new audit and rating tool we piloted in 2003 failed to meet our expectations but may prove more useful as a self-assessment tool for our suppliers. We will continue to

develop a revised rating system based around a core set of key performance indicators, the primary focus of which will be the commitment of our business partners to deliver improved workplace conditions.

In 2004 we will maintain our focus on helping our suppliers achieve self-governance. That means returning to our audit methodology and refining it so it better promotes sustainable compliance by assessing the quality of management in our suppliers' factories. With the audit results, we will continue to develop training tools that help our suppliers close the gap between what they have achieved and what they still have to do.

On page 49 of this report you can read our sustainability targets for 2004. To achieve them we will have to be at our best, and that will demand that we stay focused in the face of the challenges ahead. By working with our stakeholders and harnessing the skills and commitment of our team, I am confident we can again achieve significant progress in the coming year.



Herbert Hainer
CEO and Chairman of the Board



reach:

We aim to be a global leader in the sporting goods industry, with sports brands built on a passion for competition and a sporting lifestyle.

That means exceeding our customers' expectations. Achieving new heights of technical and design innovation. Developing our global reach.

And it means constantly setting ourselves new targets, as we strive to become a responsible, creative and rewarding organisation for all our stakeholders. In the following pages, we show how we extended our reach in 2003.

VISION AND STRATEGY /// We recognise our responsibilities for the way we do business, including the way our products are manufactured by our suppliers. Our vision is for everyone in the Group and our supply chain to share a common set of values and to follow responsible business practices. In this way we can aim to become a sustainable company.

OUR CORPORATE MISSION /// adidas-Salomon strives to be the global leader in the sporting goods industry with sports brands built on a passion for sports and a sporting lifestyle.

- We are consumer focused. That means we continuously improve the quality, look, feel and image of our products and our organisational structures to match and exceed consumer expectations and to provide them with the highest value.
- We are innovation and design leaders who seek to help athletes of all skill levels achieve peak performance with every product we bring to the market.
- We are a global organisation that is socially and environmentally responsible, creative, and financially rewarding for our employees and shareholders.

We are committed to continuously strengthening our brands and products to improve our competitive position and financial performance. This mission is rooted in our core values:

Authenticity	Passion	Innovation
Inspiration	Commitment	Honesty

These values are grounded in the reality of our business. They help us create brands that our customers believe in, and a company our stakeholders can trust.

VISION FOR SOCIAL AND ENVIRONMENTAL AFFAIRS /// As a leader in the sporting goods industry and a responsible business, our vision is to follow sustainable practices in the Group and our supply chain, and enhance the value of our brands, by:

- guaranteeing the ideals of adidas-Salomon 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.

Making this vision a reality is a challenging prospect for a company that operates a large and complex supply chain, and markets products through subsidiaries around the world. However, while we have outsourced most of our production, we have not outsourced moral responsibility for the way in which our products are manufactured and distributed.

Our goal is clear: to enhance social and environmental performance in the supply chain, thereby improving the lives of the workers who manufacture our products. Our approach is simple: to increase accountability and transparency and make the compliance process self-governing. Achieving these ends at adidas-Salomon encompasses:

A consistent set of standards It is our goal that all parts of our business, including suppliers, share a common set of values and understand how to live up to them. Our Standards of Engagement (SOE), described on page 21, play a critical role in driving the Group's values and business principles through to the supply chain.

A dedicated management team Our Social and Environmental Affairs (SEA) team is devoted to ensuring compliance with the SOE and managing related CSR activities. Ultimately, we want our business partners to go beyond simply meeting prescribed standards, to integrating them fully into their general management and decision-making processes; and finally to implement a system of self-governance.

Accordingly, our SEA team is moving away from its traditional role of policing SOE implementation to providing support and advice to our suppliers. For more on the SEA team, see page 12.

Engagement Interacting with our key stakeholders helps us to understand their concerns and interests and develop our SEA strategy and programmes accordingly. We aim to communicate with all in an atmosphere of mutual trust and respect. You can read more about our stakeholder engagement on pages 13-17.

FROM VALUES TO ACTION /// To help the adidas-Salomon Group identify and address business challenges and potential risks as early as possible, we have a structured reporting methodology.

The management team of each brand and regional business unit prepares an annual strategic business plan. This not only looks at long-term opportunities and risks, but also includes an in-depth review of likely business and social trends, such as changing customer behaviour. This enables the Group to adjust and harmonise the goals and targets of several company functions and divisions.

Social and Environmental Affairs is one such function. To complement the Group's broad-based business strategies, the SEA team follows a rolling three-year strategy that focuses on how our sustainability principles and CSR can be integrated into our day-to-day operations and work with business partners.

These strategies, together with our business principles and the results of regular interaction with stakeholders, form 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 to ensure fair and safe working conditions
3. Expanding our network of local workers' organisations, NGOs and other representative groups so that we may 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.

The SEA team's annual action plan forms the last step for putting this road map into action. Every year we translate our strategic objectives for social and environmental affairs into operational targets, and from this develop a detailed action plan of specific initiatives.

Progress is measured at fixed review dates and results are reported to the Executive Board.

SUSTAINABILITY PRINCIPLES /// Sustainability is about balancing social, environmental and economic factors to create a business with long-term potential to thrive. Our sustainability principles, based on our Group values, provide the operational framework to help us become a more sustainable company. They underpin the initiatives and performance described throughout this report.

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 Standards of Engagement. 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.

GROUP PROFILE /// With a share of around 15 percent of the world's sporting goods market, adidas-Salomon is a global industry leader. The Group consists of three major sports brands: adidas, Salomon and TaylorMade-adidas Golf. We serve wholesale and retail markets around the world, but also sponsor sports organisations, teams, individual athletes and sporting events.

OUR BRANDS /// adidas-Salomon offers consumers a broad range of sports brands across all sport categories, in all markets.

adidas is a leading brand in the sporting goods market with strong positions in footwear, apparel and hardware. The adidas brand is structured in three divisions: Sport Performance, Sport Heritage and Sport Style.

Salomon is our Freedom Action Sports brand. With leading positions in alpine, nordic and snowboard products, Salomon is actively expanding its presence in summer and alternative sports as well as soft goods. The Salomon family of brands comprises Salomon, Mavic-adidas Cycling, Arc'Teryx, Bonfire and Cliché.

TaylorMade-adidas Golf covers a full range of golf hardware, footwear, apparel and accessories. It markets products under the brand names TaylorMade, adidas Golf and Maxfli.

OUR OFFICES /// The Group and its more than 100 subsidiaries are directed from our headquarters in Herzogenaurach, Germany. Also based in Herzogenaurach are the business units for running, football and tennis as well as the major part of our research and development department.

Other key corporate units are based in Portland Oregon, USA – the home of adidas America Inc, and the basketball, adventure and alternative sports business units. The golf business unit is based in Carlsbad, California, USA, and the winter and 'Freedom Action Sports' business units are headquartered in Annecy, France.

The Group also operates design and development departments in other locations around the world, corresponding to their business activity.

adidas-Salomon International Sourcing Ltd (aSIS), a fully-owned subsidiary with headquarters in Hong Kong, is responsible for worldwide sourcing. aSIS sourcing offices are located in Brazil, China, Indonesia, Korea, Pakistan, Singapore, Taiwan, Thailand, Turkey, USA and Vietnam.

OUR EMPLOYEES /// At December 31, 2003, adidas-Salomon employed 15,686 people. This represents an increase of seven percent from the previous year. In 2003, the largest number of new employees came from the retail sector.

adidas-Salomon employees represent a cross-section of cultures, ages and backgrounds. Women account for 45 percent of our employees. Of the executive management positions, women hold 23 percent and 77 percent are held by men. Because a generally accepted definition for minorities does not exist in Europe, adidas-Salomon is unable to provide such data. At our headquarters in Herzogenaurach, we have employees from over 40 countries with an average age of 33. For more detail about our employees, please see our 2003 Annual Report.

SHARE LISTING /// The adidas-Salomon share is listed on the Frankfurt Stock Exchange in Germany. The stock is a member of the DAX-30, Germany's premier stock index.

SUPPLIERS /// adidas-Salomon works with independent suppliers from around the world who manufacture our products. 60 percent of all factories are located in Asia, with 20 percent in the Americas and 20 percent in Europe and Africa.

LICENSEES /// For some product segments or markets, adidas-Salomon has licensing agreements with independent companies, which manage the design, development, manufacture and distribution of specific product lines. Currently adidas has 18 licensees that source products from 154 suppliers in 24 different countries.

FINANCIAL PERFORMANCE /// Sustainability is as much about long-term financial stability and growth as it is about social and environmental performance. The tables on page 10 show our financial performance in 2003 and compare this with the previous two years.

Total number of adidas products manufactured¹

Product Range	2003	2002	2001
Footwear (millions of pairs)	111.29	99.57	81.60
Apparel (millions of units)	146.72	129.30	125.60
Hardware ² (millions of units)	27.63	24.43	17.90

¹ International range excluding Salomon, TaylorMade and Mavic sports equipment

² Accessories and gear

Total number of Salomon Softgood products manufactured¹

Product Range	2003	2002	2001
Footwear (millions of pairs)	2.99	2.34	3.00
Apparel (millions of units)	0.60	0.51	0.66
Accessories + gear (millions of units) (bags, gloves and caps)	0.87	1.02	1.48

¹ International range excluding Salomon hardgoods e.g. skis, boards, bindings

Total number of Salomon products manufactured

Product Range	2003	2002	2001
SNOWBOARD (MILLIONS OF UNITS)			
Board	0.11	0.12	0.13
Binding	0.13	0.12	0.12

ALPINE (MILLIONS OF UNITS)

Ski	0.72	0.74	0.83
Binding	1.21	1.30	1.30
Boots	1.19	1.14	1.10

CROSS-COUNTRY (MILLIONS OF UNITS)

Binding	0.83	0.68	0.80
Boots	0.46	0.46	0.38

TEC HIKING (MILLIONS OF PAIRS)

Boots	0 ¹	0.07	0.20
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INLINE SKATES (MILLIONS OF PAIRS)

ILS	0.46	0.31	0.62
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MAVIC (MILLIONS OF PAIRS)

Rims	1.56	1.70	1.63
Wheels	0.55	0.45	0.39

¹ Number of Tec Hiking boots 2003 is included in Salomon Softgoods/Footwear.

Total number of TaylorMade-adidas Golf products manufactured¹

Product Range	2003	2002	2001
TAYLORMADE HARDWARE (MILLIONS OF UNITS)			
Woods	2.10	1.45	1.11
Irons	2.82	1.66	2.06
Putters	0.29	0.18	0.14
Kids Clubs	0.03	0.01	0.01

TAYLORMADE SOFTGOODS (MILLIONS OF UNITS)¹

Bags	0.33	0.17	0.06
Gloves	1.80	0.28	0.13
Balls ²	4.46 ³	4.49 ³	0.51
Caps	0.61	0.32	0.17
Accessories	1.11	0.38	0.18

¹ Excluding adidas Golf

² Reflected as dozens

³ Balls produced by Dunlop Slazenger

Net sales by brand

Net sales (euros in millions)	2003	2002	2001
adidas	4,950	5,105	4,825
Salomon	658	684	714
TaylorMade-adidas Golf	637	707	545

Net sales by region

Net sales (euros in millions)	2003	2002	2001
Europe	3,365	3,200	3,066
North America	1,562	1,960	1,818
Asia	1,116	1,166	1,010
Latin America	179	163	178

Net sales by main product divisions

Net sales (euros in millions)	2003	2002	2001
Footwear	2,767	2,851	2,650
Apparel	2,222	2,288	2,212
Hardware	1,278	1,385	1,250

Operating highlights

Operating highlights (euros in millions)	2003	2002	2001
Net sales	6,267	6,523	6,112
Income before tax	438	390	376
Net income	260	229	208

Key ratios (%)

Gross margin	44.9	43.2	42.6
Selling, general and administrative expenses as a percentage of net sales	35.5	34.4	33.3
Effective tax rate	38.0	37.9	39.0
Net income as a percentage of net sales	4.2	3.5	3.4
Equity ratio	32.4	25.4	24.3

Per share of common stock (euros)

Basic earnings per share	5.72	5.04	4.60
Dividend per share	1.00 ¹	1.00	0.92
Share price at year end	90.30	82.30	84.30

Number of shares outstanding	45,453,750	45,422,500	45,349,200
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Rounding differences may arise in percentages and totals for figures presented in millions, as calculation is based on figures stated in thousands.

¹ Subject to Annual General Meeting approval

CORPORATE GOVERNANCE /// Corporate governance refers to standards of good and responsible corporate management. Good corporate governance and transparent communication have always been a priority for our Group.

ESTABLISHING CORPORATE GOVERNANCE PRINCIPLES /// The adidas-Salomon Corporate Governance Principles are designed to help us manage the business responsibly – with the emphasis on added value – and promote stakeholder confidence in the Group. The Corporate Governance Principles also address: the rights of the shareholders, the responsibilities and duties of the Executive Board and the Supervisory Board, and how they collaborate; information and disclosure obligations; and the solution of any conflicts of interest.

These Principles were approved in 2003 by the Executive and Supervisory Boards, and are based on the German Corporate Governance Code as well as on the recommendations of other internationally recognised codes of practice. For more documents on Corporate Governance at adidas-Salomon, please see our website www.adidas-Salomon.com/en/overview/corporate_governance/

THE EXECUTIVE AND SUPERVISORY BOARDS /// The Executive Board comprises six members (status as of December 31, 2003) – individuals who reflect the diversity and international nature of the Group. It formulates the strategy and direction of the Group, agrees this with the Supervisory Board and ensures that this strategy is put into practice. It is also responsible for ensuring that the appropriate risk management and risk monitoring procedures are in place, and guarantees the observance and development of the Group's internal standards, policies and strategies.

The Supervisory Board advises and supervises the Executive Board in the management of the 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.

The Supervisory Board is composed of 12 members, six of whom are elected by shareholders at the Annual General Meeting and six who are elected by the employees, according to the German Co-Determination Act (MitBestG). As the term of office of the current Supervisory Board members will expire at the end of the Annual General Meeting in May 2004, new elections will take place in 2004.

SHAREHOLDERS /// Shareholders in adidas-Salomon AG exercise their voting rights at Annual General Meetings. They are kept informed of the Group's activities and performance through a financial calendar, the annual report, quarterly reports and our annual Social and Environmental reports.

WORKS COUNCILS /// The Group has established Works Councils at adidas-Salomon AG in Germany and in other European subsidiaries.

Headquarters (HQ) Works Council In 2003, the HQ Works Council focused on the following projects:

- Salary and remuneration structure
- Revision of internal agreements on flexible working time
- Work-Life Balance
- Modification of the Group pension fund/retirement benefits
- Flexible, part-time retirement.

European Works Council The European Works Council, consisting of 13 delegates in nine European countries, held one annual meeting and the steering committee met on two occasions in 2003.

There is a fruitful collaboration between the European and HQ Works Council and the SEA team. 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. During 2003, members of the Works Council were also invited to participate in several stakeholder meetings. The HQ Works Council ran training sessions on co-determination and worker-management communications for the SEA team, and provided advice on request.

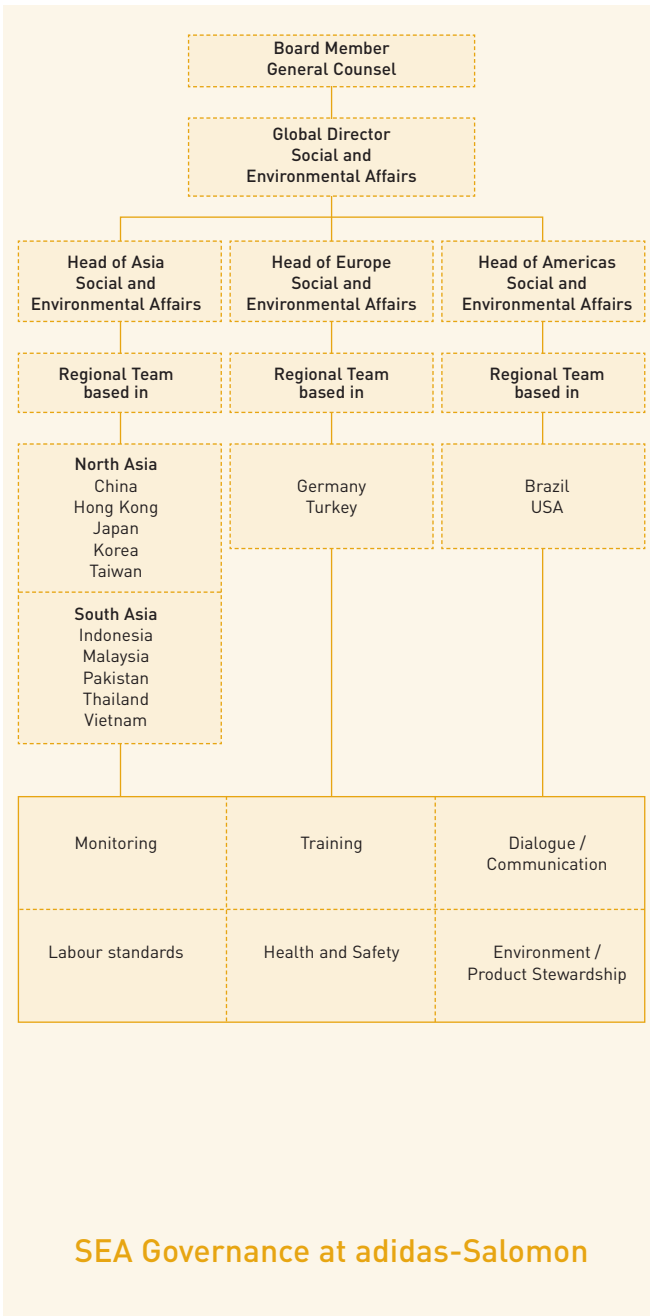
To further improve transparency and communication, employees have a direct channel to the management team for Global Operations, via a Q&A hotline called 'Ask the Management'. This enables employees to submit questions and concerns anonymously, by email. Management's response to the individual questions is posted on the Group's intranet site.

RISK MANAGEMENT /// The governing principles we have established ensure good management and control of the business. However, no formal system of governance can prevent high-risk behaviour or potential damage to a company and/or society, unless people within the organisation share a clear understanding of the risks and challenges faced.

adidas-Salomon faces a variety of global and local business risk factors. These risks can be internal or external, and if not appropriately managed may impact the Group's goals, strategies, brand image, or financial performance and health. To address these risks, adidas-Salomon has created and uses a comprehensive risk management system, the major elements of which include:

- Fully integrating risk management into day-to-day business functions at all organisational levels
- Configuring our organisation to allow for early identification, analysis and evaluation, effective communication and management of risk. This requires suitable action for risk avoidance, reduction, transfer or acceptance, and continuous monitoring
- Preparing and implementing an appropriate reporting structure and contingency plans to reduce the potential risk impact to an acceptable level
- Requiring participation in risk management from managers and employees at all levels of the Group. In particular, the Executive and Supervisory Boards support the development of a pro-active, forward-looking risk management culture within all brands and regions.

More information about the group's risk management system can be found on our website www.adidas-Salomon.com/en/investor/strategy/risk_management/



FROM GOVERNANCE TO ACTION /// Every year the Executive Board prepares a strategic business plan, which must be approved by the Supervisory Board. This plan not only anticipates business opportunities and threats, but also standardises goals and targets across various corporate functions and divisions. The SEA Department is one such function. It is headed up by the Global Director who reports directly to the company's Legal Counsel and Board Member, Mr Manfred Ihle. You can see how the SEA team is structured in the adjacent diagram.

The SEA team produces its own three-year rolling strategy, an annual action plan, and writes monthly progress updates for the responsible Board member. These updates keep the Board informed of current social and environmental issues and risks along the supply chain.

The primary focus of the team is to work with suppliers to secure compliance with the SOE. In 2003 the team consisted of 32 people. It is a diverse group of individuals with a variety of educational backgrounds and professional experience, including law, engineering, finance and human resource management. The team is organised into three regional teams covering Asia, the Americas and Europe. Whenever possible, our field auditors come from the communities in which they are working, and have first-hand knowledge of the local language and culture. This enables us to communicate more effectively with our suppliers and with the workers employed by them.

The SEA team collaborates closely with Global Operations, which is responsible for the development and sourcing of products from our suppliers. At times the SEA also serves as an adviser to other units in the company, including Marketing, Product Development, Human Resources, Facility Management, Legal, Investor Relations and Licensing.

To keep pace with changes in our sourcing organisation we restructured the SEA team in Asia during 2003. Three existing sub-regional teams were merged and re-organised into two distinct units: North Asia and South Asia, each led by a regional manager. Following a matrix arrangement, team members in Asia also work alongside two discipline leaders, specialists who have region-wide responsibilities for labour compliance and occupational health, safety and environment. These changes took effect in October 2003 and allow us to work more closely with our sourcing organisation and our main suppliers, and to strengthen our advisory and training work.

CODE OF BUSINESS ETHICS AND CONDUCT FOR EMPLOYEES ///

We have a Code on Business Ethics and 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. The Code outlines the key principles employees should follow, and how they should respond to different situations in their work and daily business dealings. It provides direction on issues such as corruption and bribery, loans, gifts and conflicts of interest. We have shared the content of our Code with our business partners, so that they understand our expectations and our ethics.

OUR STAKEHOLDERS /// To ensure our social and environmental programme is effective and develops appropriately, regular stakeholder dialogue and feedback is essential.

WHO ARE OUR STAKEHOLDERS? /// Our stakeholders are the organisations, groups and individuals whom we affect and who affect us. They are a diverse group, including employees, suppliers, consumers, investors, customers and non-government organisations. For a full list of our stakeholders see page 14.

WAYS WE ENGAGE ///

Multi-stakeholder dialogues In 2002 we began formal stakeholder consultation meetings ('dialogues') to canvass the views of our key stakeholders. These dialogues supplement the many individual points of contact, meetings and enquiries that we have throughout the year. Dialogues held last year focused on securing feedback on our SOE programme (see page 16).

Multi-stakeholder dialogues were held last year in our Asia and Europe regions. Region Americas did not schedule a formal dialogue but is preparing several engagements with workers in 2004.

A full record of our past stakeholder dialogues is posted on our webpage at www.adidas-Salomon.com/en/sustainability/

Asia Our Asian regional stakeholder dialogue took place in Guangzhou, China in November 2003. Sixteen representatives from NGOs, trade unions, universities, the ILO and our own suppliers (including both management and workers) took part. Staff from China Development Brief, Beijing acted as independent observers and provided a supplementary report on processes and alternatives.

Given that dialogue of this nature is still fairly new in China, the discussions were broad-ranging and for the most part went 'back to basics'. For example, participants were very keen to discuss what corporate social responsibility (CSR), as an imported concept, means in China and how it relates to indigenous concepts. Further, it became clear that while obtaining direct feedback from worker representatives is essential, this was not the right forum in which to do it.

Europe The European stakeholder consultation meeting was held in Brussels, Belgium in October 2003. A diverse range of organisations was invited, including the European Trade Union Federation of Textile, Clothing and Leather, an NGO, the Foreign Trade Association (FTA), a financial analyst and a competing brand.

Participants felt the Group's long-term move from supplier monitoring to self-governance was innovative. They also considered it important for adidas-Salomon to continue to work with other companies, the ILO and local organisations on building capacity in the supply chain.

Most participants agreed that next time, the audience should be extended to include representatives from government, consumers, suppliers, the environmental lobby, other challenging NGOs and the media.

Outcomes Based on feedback from these meetings, the design of future dialogues will take into account the following:

- Inviting a broader audience including government and consumer groups
- Focus groups facilitated by adidas-Salomon must be action-oriented, developing plans which will further the implementation of CSR within the Group.

Structured worker dialogues The people who produce our products are an important part of our stakeholder community but we do not always hear their voices. To better understand their concerns, we piloted two worker dialogues – one in Portugal and one in Turkey.

Workers from a cross-section of apparel factories were asked to provide their general views on codes of conduct and to comment on factory-specific compliance issues. An independent third party facilitated each meeting. adidas-Salomon SEA staff attended as observers.

While these meetings had different dynamics and represented a small percentage of workers in our global supply chain, the general outcome was more or less the same. No severe compliance issues were revealed, but it is clear that communication is a major issue – with top-down and bottom-up methods not always working.

We will revise the approaches taken this year and identify more effective ways to get workers engaged in our SEA programme. We are planning more worker dialogues for Asia and the Americas in 2004.

Employee engagement Staff surveys in 2002 highlighted two clear deficiencies in our SOE programme – the need for SOE training at all levels in the Group, and for wider distribution of the annual Social and Environmental Report. In 2003, we addressed these issues through the following activities:

Induction for new employees In Asia, a description of the SOE programme was included in an induction booklet issued to new employees. In Europe, all new employees were invited to orientation seminars and given a copy of the Social and Environmental Report. A similar but less formal process took place in the Americas.

Raising awareness of the Social and Environmental Report

The 2001 and 2002 Social and Environmental Reports were published and announced on the same day as the Annual Report. It was communicated to all employees via our global newsletter, and posted on our intranet and website.

Training

- In the Americas, SEA regional staff held eight compliance training sessions for regional quality control staff in Central America and sourcing liaison offices in the US and Brazil.
- In Europe, SEA team members held 10 training sessions with quality control staff, sourcing liaison office staff in Turkey, subsidiary employees from aFrance, altaly, aSouth Africa, aMoscow, Salomon Romania, and an adidas licensee.
- In Asia, the SEA team provided 14 training sessions for internal staff in Guangzhou, Hong Kong, Indonesia, Singapore, Thailand and Vietnam. There were also SOE training sessions for subsidiaries in India and the Philippines.

At the end of 2004 we will again survey staff views on the application of SOE and the Group's general approach to CSR.

OUR STAKEHOLDERS

AUTHORISERS ///

Government
Trade associations
Shareholders
Board of Directors

BUSINESS PARTNERS ///

Employees
Unions
Suppliers
Workers
Distributors
Service providers

OPINION FORMERS ///

Journalists
Community members
Special interest groups

CUSTOMERS ///

Professional sports people
Distributors
Retailers
Individuals

As part of our stakeholder engagement programme, we invited CSR Network Ltd to review our reporting and give us feedback. CSR Network is a business-focused corporate social responsibility organisation, bringing together specialists from the fields of environmental management, social accounting and sustainable development. Their commentary is reproduced here.



Independent review of adidas-Salomon Social and Environmental Report

CSR Network has not been commissioned to act as independent assurance providers and our views have not been based upon an independent review of management systems, data quality or stakeholder expectations.

During 2003 adidas-Salomon asked CSR Network to comment on its 2002 Social and Environmental Report (SER) 'Behind our Brand' in the context of emerging best practice in reporting and also within the context of the Global Reporting Initiative (GRI) 2002 Sustainability Guidelines.

In response, we benchmarked the 2002 report using the criteria applied for 'Material World' - CSR Network's report on its 2003 benchmark survey of the largest 100 global companies (by revenue). Based on this assessment, adidas-Salomon reporting approaches best practice. The 2002 SER ranked only just outside the top 10 reporting companies in the Survey overall. It included a detailed map of their reporting against GRI guidelines' recommended contents and indicators. The company has adopted the incremental approach towards reporting 'in accordance with' GRI guidelines, and the GRI core performance indicators are used pro-actively by the company to identify gaps in its reporting.

Overall, the 2002 report presents a clear corporate vision. It details policies and management processes, and includes a concise description of relevant corporate governance issues. In our view, there was also comprehensive reporting of

stakeholder engagement programmes, processes, feedback and response by adidas-Salomon.

The company's social and environmental reporting focused on its supply chain, emphasising management of social and ethical issues and relevant performance. This focus derives from the company's view that the majority of its social and environmental impacts lie in its supply chain. However, we felt that adidas-Salomon could enhance its reporting by including more detail of how it applied its social and environmental policies to its own sites, operations, products and employees. The benefits of this approach would be to demonstrate to its suppliers how the company 'walks the talk' and also to substantiate the focus on supply chain issues.

In this 2003 SER the scope remains focused upon the supply chain; however adidas-Salomon have responded positively to our observations. The report maintains its previous high standards and now includes additional reporting on risk management, the code of business ethics and conduct for employees, a presentation of employee data relating to gender and culture, and the work to develop an adidas-Salomon policy on donations. These were all issues that we felt should be covered in more depth.

In our view the 2002 SER did not fully present the company's work on issues around sustainable product management and only hinted at its Integrated Product Policy (IPP) initiatives. This 2003 report gives a more complete description of adidas-

Salomon policy and actions regarding environmental impact of its products, taking into account the whole life cycle.

Management of ethical issues in a multi-tiered supply chain remains controversial within the sports and wider apparel sector. Development and implementation of a suitable, performance based approach to rating supplier social and environmental performance is particularly challenging. In its 2002 SER, adidas-Salomon described its continuing efforts to develop its five-star rating system for supplier auditing. In the period since that report, the company reports that it has explored an alternative and more detailed audit-rating tool. In this 2003 Report, the company says that it will maintain the original rating system, based upon the results of comprehensively field-testing the alternative. In our view, the continuing credibility of adidas-Salomon's work on social and environmental performance management and reporting will largely be dependent on the successful conclusion and roll-out of its preferred approach to auditing in the coming years.

Finally, adidas-Salomon has recognised the value of ongoing, comprehensive and effective stakeholder dialogue. Pursuing this approach in future will enable the Group to anticipate and respond to emerging issues and also to ensure that future reports remain aligned with external expectations.

CSR Network Ltd, U.K., 2004
www.csrnetwork.com

STAKEHOLDER FEEDBACK ///

Feedback on the SOE programme One of the primary goals of the multi-stakeholder dialogues that took place in 2003 was to gather feedback on our SOE programme. The following is a summary of what we were told:

General

- Participants felt adidas-Salomon should take a lead in CSR and build brand reputation in line with our position as a sports industry leader.
- CSR standards should be localised in both language and content. However, adidas-Salomon should collaborate with other brands and NGOs to create a single worldwide standard.
- CSR should be a pre-condition in selecting suppliers and factories.
- Multi-national companies such as adidas-Salomon should be involved in responding to the HIV/AIDS issue.

Engagement

- A mechanism is needed to ensure workers are directly involved in the SOE process. This is particularly important in China, where workers are governed by factory rules rather than national law.
- adidas-Salomon should work with governments and trade unions to promote CSR.
- A global Works Council should be established to provide a forum for all adidas-Salomon employees.

Training and capacity building

- Best practice training should be promoted and shared between factories. Brands should practice more collaboration in training and capacity building.
- Management and workers should be encouraged to develop stronger problem-solving skills. More support should be given to the small-medium suppliers to raise their level of compliance.

RESPONDING TO FEEDBACK ///

Follow-up to 2002 feedback Feedback from the 2002 stakeholder meetings was incorporated into our plans for 2003, but we did not achieve all that we aimed for. For example, our termination policy remains to be published, and we were unable to increase the transparency of our grading system by partnering with an NGO. Only one of the two formal Asia region stakeholder dialogues planned in 2003 was held, although the postponed second meeting is now scheduled for the first quarter of 2004.

We did, however, achieve the following:

- An external consultant reviewed the 2002 report, and those recommendations are reflected in this report.
- The outcome of the Fair Wage Study was discussed with a broader audience, as described on page 34.
- The number of independent audits required by the Fair Labor Association (FLA) was exceeded.
- An independent third-party audit of one of our football production facilities in China was commissioned.
- A member of adidas-Salomon HQ Works Council/European Works Council participated in the European stakeholder meeting.
- Measurement of the environmental impact of footwear production was improved, as explained on page 39.

Follow-up to 2003 feedback We have taken into account the feedback received from multi-stakeholder and worker dialogues held in 2003, and incorporated this into our strategies and targets for 2004. Specific areas to be addressed next year include:

- In addition to the larger and more diverse dialogues, we will conduct smaller, targeted dialogues with specific stakeholder groups to address individual issues of concern and map action plans which participants can directly influence.
- We will make the multi-stakeholder dialogue in Europe more interactive by inviting adidas-Salomon employees from other corporate functions, and achieving a better balance between social and environmental interests.
- In Asia, where stakeholders are less familiar with CSR concepts and consultation processes, we will better prepare participants for the discussions, and our expectations regarding their involvement.
- The Group will improve the dialogue with government officials, both within the departments of host nation governments and at the embassy or consular level.
- Individual projects relating to worker health – in particular HIV/AIDS education and prevention – will be rolled-out more widely in 2004, following key pilots which began in 2003.
- The SEA team will help develop a Corporate HIV/AIDS policy for the adidas-Salomon Group.
- adidas-Salomon will participate in a multi-stakeholder initiative in Bulgaria to build capacity within the apparel industry.
- Specific worker dialogues will be held in north and south Asia in 2004.

Responding to enquiries During the year, we have responded to various enquiries from the media, NGOs, workers rights groups, campaigners, academics and our suppliers, on topics related to the SOE programme and current practice and conditions within factories. Examples include:

- Allegations by an NGO group concerning working conditions in a garment factory in El Salvador
- Concern over workers left without jobs, following the sudden closure and disappearance of a garment factory in Thailand in 2002
- The continued use of kangaroo leather in the manufacture of soccer boots
- Freedom of Association issues in Honduras and El Salvador.

Where such concerns have been raised these have been fully investigated, assessed and a response issued. Details of our responses can be found at: www.adidas-Salomon.com/en/sustainability/

Maturing relationships Relationships with some of our more vocal critics have matured and new levels of understanding and cooperation have been achieved through closer engagement with non-governmental organisations. For example:

- In December, a Hong Kong-based NGO that focuses on worker rights in China, facilitated a round table discussion in Guangzhou between the compliance staff of the major sporting brands on the issue of freedom of association. The workshop has led to the companies agreeing on joint actions to improve management-worker communications and worker representation in China.
- adidas has been working with the Workers Rights Consortium (WRC) to address labour issues and improve workplace conditions at PT Dada (one of our cap suppliers) in Indonesia since 2002. These efforts were expanded in 2003, with an investigation of an Indonesian garment factory supplying an adidas licensee.
- While our relationship with Marie Stopes International (MSI) has centred around worker health issues in Vietnam, we are now discussing how to expand our work with MSI to China, where the organisation fulfils a unique role in providing health services and information to youth and lower socio-economic groups. On page 33 we provide a case study of our relationship with Marie Stopes in Vietnam.
- In 2003, we strengthened our relationship with CARE in Cambodia by providing financial support for the training of expatriate Chinese supervisors based in the Cambodian apparel factories. The training subjects include cultural sensitivity and awareness, basic instruction in Khmer, and the importance of health & safety training for production line workers. In 2004, the SEA team will use the training as a pilot to pursue similar activities in other countries in the Asia region.

Participation and collaboration We continue to contribute to and comment on industry best practice relating to stakeholders, through our membership of organisations such as the World Business Council for Sustainable Development, Business for Social Responsibility, the World Federation of Sporting Goods Industry and the FLA. We have also participated in:

- A European Multi-stakeholder Forum on CSR
- A Forum on Worker Complaint Mechanisms held in the Netherlands
- Consultations on the World Bank's research on strengthening implementation of CSR in global supply chains
- Dialogues with fund managers and analysts from leading German, French and English Socially Responsible Investment funds.

Sharing knowledge with other brands The SEA team is in regular contact with their counterparts in other companies, discussing common issues and sharing information and best practice. Examples of brand-level collaboration during 2003 included:

- Shared FLA audits – adidas-Salomon worked with four other brands on the remediation plans for six shared factories and continued to share visits with other brands on remediation follow-up.
- Joint brand meetings in Asia, the Americas and Europe. For example, in Hong Kong, SEA team members joined senior compliance staff from Nike and Reebok to discuss opportunities for synergies in their compliance programmes.

SUPPLIERS /// In 2003 we continued the process of consolidating our supply chain, particularly for adidas-branded products for the export market, by placing larger orders with fewer factories. We believe that developing closer relationships with our business partners will improve the quality of the product. We also believe that deepening our relationships with business partners will lead to a higher level of compliance with the SOE, and we have restructured the SEA team in Asia to help achieve this.

As part of the consolidation process, we have strengthened our reporting and accounting processes to better identify the suppliers and licensees we deal with. As a result, we have actually recorded an increase of the numbers of suppliers and licensees within several of our brands.

SUPPLY CHAIN STRUCTURE /// Our supply chain is complex: it is global in its coverage and multi-layered. We have many different types of business partner, some of whom we have direct business relations with, others not. In general, we can better communicate our SOE to those suppliers who have a direct contractual relationship with adidas-Salomon.

Overall we rely on about 900 factories around the world. The group itself owns eight factories, in Germany, France, the United States and China. Some 60 percent of our suppliers are based in Asia. Of the remaining factories, 20 percent are based in the Americas and 20 percent in Europe. By comparing our supplier numbers with last year, we can see we have:

- 78 more suppliers overall, including an increase of 36 licensee factories
- Significantly more suppliers in: China 60, Korea 37, USA 21, Taiwan 13, South Africa 10, Brazil 8
- Significantly fewer suppliers in: Turkey 17, Portugal 13, Mexico 8, Malaysia 7, Hungary 6, UK 5

SOURCING STRATEGY /// The Group's sourcing strategy aims to consolidate the supplier base and focus primary export production in a handful of key sourcing countries, notably China, India, Indonesia, Thailand, Turkey and Vietnam. Such consolidation will strengthen business relationships with our long-term strategic partners, as they will enjoy greater stability and certainty in orders placement and will be better placed to plan future investment in equipment and facilities. We believe that this will also enhance our leverage and the level of SOE compliance.

TYPES OF SUPPLIER /// Our suppliers range in size from publicly listed companies, employing over a quarter of a million employees with production in multiple countries, to small family-run businesses, employing less than 10 people. They fall into four broad categories:

Main factories Factories of suppliers that have a direct contractual relationship with adidas-Salomon for the supply of products, whether for export or domestic market consumption. We call these Tier 1 suppliers. Most of our Tier 1 suppliers produce for many brands. Some of our largest Tier 1 suppliers have multiple factories and manufacturing sites.

Subcontractors Factories that have been subcontracted by our suppliers and do not have a direct contractual relationship with adidas-Salomon. They work directly for the main factories.

Material and other service providers These suppliers may not have a direct business relationship with adidas-Salomon, but supply goods and services to our main suppliers. Known as Tier 2 suppliers, these companies vary hugely in their size and operation – from a printer with five employees screen-printing t-shirts, to an international fabric mill employing hundreds of workers.

Within this category, there are nominated material suppliers with whom we work. Nominated material suppliers are required to adhere to the strict standards of the company's 'A-01' material testing policy. This same policy also requires nominated suppliers to comply with the SOE.

Licensees Independent companies who manage the design, production and distribution of specific product lines, under license to the adidas-Salomon group.

We have developed a standard reporting and compliance protocol that details how our licensees and their supply chains are to comply with the SOE. Under this protocol, licensees must establish their own compliance programmes based on the tools and guidance materials developed by the SEA team. Where a licensee does not have the resources to recruit and train their own compliance teams, they are required to engage reputable external auditors to monitor and support remediation at the factory level.

Number of suppliers and our own factories in 2003¹

Region	No. of suppliers (excl. own factories)	No. of own factories	Total
ASIA			
adidas	484	1	539
Salomon ²	12	0	
TaylorMade-adidas Golf ³	41	1	
AMERICAS			
adidas	148	0	183
Salomon ²	11	1	
TaylorMade-adidas Golf ³	22	1	
EUROPE			
adidas	168	1	184
Salomon ²	12	3	
TaylorMade-adidas Golf ³	0	0	
Total	898	8	906

¹ Includes licensee factories

² Includes Bonfire, Mavic, Arc'Teryx and Cliché

³ Includes Maxfli

adidas licensees in 2003

Product Range	Total no. of licensees	Total no. of factories producing for licensees	No. of countries where production is placed
Apparel	11	103	19
Hardware ¹	4	23	8
Watches	1	25	2
Glasses	1	2	2
Cosmetics	1	1	1
	18	154²	

¹ Accessories and gear

² The 154 factories are located in 24 different countries



The SEA management cycle

WORKING WITH SUPPLIERS /// Our strategy is based on a vision of long-term self-governance and our goal is sustainable compliance. Consistent with this approach, the SEA team is progressively moving away from its traditional role of being an inspectorate policing a code, to one of providing support and advice to our suppliers.

This does not mean that we no longer monitor. Rather, it means that the SEA team is moving away from monitoring issues, to monitoring the performance and efficiency of the management team and systems in our partner factories. In particular, we are looking for well-structured health, safety and environment and human resource systems, with qualified, committed and capable middle managers, supported and empowered by senior management.

Ultimately, suppliers and their employees must take ownership of the compliance programme to ensure long-term execution and consistency.

To achieve this, the SEA team's auditing techniques will be upgraded to:

- Better identify the causes of any gaps in a supplier's compliance performance
- More closely evaluate management's commitment to compliance
- Build a more detailed picture of supplier's business systems and practices.

These measures enable us to develop more relevant action plans and remediation.

The next step in the cycle is the promotion of management systems and compliance strategies. Suppliers will be obliged to develop a strategy and roadmap for compliance. As mentioned previously, they must also implement formal HSE and HR management systems and retain effective administrators for these systems. Ongoing integration of the initiatives for the SOE and the Lean Manufacturing programme will be integral to this effort.

We believe that this progression of activities promotes sustainable compliance. Suppliers who are committed to compliance, who have implemented appropriate and effective management systems, and who maintain supportive training programmes, will complete the sustainable cycle with self-assessment auditing exercises. The SEA team is developing key performance indicators that will analyse results from each step of the upgraded management cycle, and support internal reporting criteria for supply chain performance. The SEA management cycle that underpins this approach is depicted in the adjacent diagram.

Standards of Engagement: Authenticity / Inspiration Passion / Commitment Innovation / Honesty

These are the core values of the adidas-Salomon Group. We measure ourselves by these values and we measure our business partners in the same way.

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

The Standards of Engagement are tools that assist us in selecting and retaining business partners who follow work place standards and business practices aligned with our policies and values. As guiding principles, they help identify potential problems so that we can work with business partners to address issues of concern as they arise. Business partners must develop and implement action plans for continuous improvement in factory working conditions. Progress against action plans will be monitored by business partners themselves, our internal monitoring team and external independent monitors.

Specifically, we expect our business partners to operate work places according to the following standards and practices.

GENERAL PRINCIPLE

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

EMPLOYMENT STANDARDS

We will do business only with business partners who treat their employees fairly and legally with regard to wages, benefits and working conditions. In particular, the following standards apply:

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.

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 make recruitment and post-hiring decisions based on ability to do the job, rather than on the basis of personal characteristics or beliefs. Business partners must not discriminate in hiring and employment practices on the grounds of race, national origin, gender, religion, age, disability, marital status, parental status, association membership, sexual orientation or political opinion.

Wages and Benefits Wages are essential for meeting the basic needs of employees and reasonable savings and expenditure. In all cases, 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.

Wages must be paid directly to the employee in cash or check or the equivalent. Information relating to wages must be provided to employees in a form they understand. Advances of, and deductions from, wages must be carefully monitored and comply with law.

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.

Hours of Work 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 and 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. Where law specifically restricts the right to freedom of association and collective bargaining, business partners must not obstruct alternative and legal means for independent and free association or collective bargaining. Additionally, business partners must implement systems to ensure effective communication with employees.

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.

HEALTH AND SAFETY

A safe and hygienic working environment must be provided, and occupational health and safety practices which prevent work-related 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 that 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.

COMMUNITY INVOLVEMENT

We will favour business partners who make efforts to contribute to improving conditions in the countries and communities in which they operate.





respond:

On paper, it's easy to plan the way forward.
On the ground, things are rarely that simple.

In this section we look at how, by balancing the needs of all our stakeholders and responding to challenging local conditions, we continue to make progress – and help our suppliers make our standards a workable reality in their factories.

IMPROVING THE WAY WE WORK WITH SUPPLIERS /// In the previous section, we described our business, strategy and relationships with stakeholders and suppliers. In this section we report on our progress in delivering our strategy of sustainability and self-governance within our supply chain.

Key initiatives in 2003 that supported our sustainable compliance strategy included:

- Holding management level meetings with all our major footwear partners and selected key apparel suppliers, to discuss and agree to a long-term compliance strategy for their businesses.
- Re-examining and refocusing our compliance work and audit tool. This helped us understand that greater emphasis must be placed on identifying and remedying the root causes of non-compliances.
- Developing an action plan for the roll-out of health, safety and environmental (HSE) management systems training and certification requirements in 2004.
- Assessing our suppliers' training needs, focusing on the qualification and experience of individuals in human resource (HR) and HSE roles.
- Identifying potential strategic partners for delivering HSE and HR management systems.

During the year we faced a number of constraints that hampered our efforts to fully meet our objectives and work plans. The SARS crisis led to a company-wide ban on travel to Asia; subsequently, audits and follow-up visits to the Chinese factories were curtailed for two months. The ongoing war on terrorism, war with Iraq, and bombings in Indonesia and Turkey further restricted regional travel by SEA team members. The result was that training activities were compressed into the fourth quarter of 2003, and some were postponed until 2004. A number of planned audits in Asia were cancelled, and the South Asia Stakeholder Meeting was rescheduled for 2004.

The SEA management cycle (depicted on page 20) follows a four-stage process:

1. Setting and explaining our standards
2. Auditing compliance with our standards
3. Promoting management systems
4. Providing training and guidance.

In the rest of this chapter, we use this structure to review our progress in improving supplier performance in 2003.

SETTING AND EXPLAINING OUR STANDARDS /// Through our Standards of Engagement (SOE) (see page 21) we have established a global set of standards for all our suppliers. Supplementing the SOE are guidelines on employment, HSE and environmental best practice. These form the basis for all our work with suppliers.

However, we have to respond to local conditions in the countries where our suppliers operate and identify different ways to approach the application of our standards. This is illustrated below by our maturing approach to freedom of association (FOA). We also recognised that we needed to provide more support to suppliers who fell short of our standards, and revised our approach to the way we enforce our standards.

Finding different ways to promote FOA Our position on the FOA and Collective Bargaining standard had always been neutral, i.e. neither pro- nor anti-union. We believed, and still believe, that it is paramount to protect the rights of workers to freely associate, and to ensure that no worker at an adidas-Salomon supplier facility suffered because of his or her union affiliation or activity. In the past, this has meant persuading factory management to rehire workers dismissed for attempting to form workers' associations, and in extreme cases supporting the release of jailed union officers, as in the case of Ngadinah Binti Abu Mawardi of Perbupas Union at PT Panarub, Indonesia.

At the start of 2003, we examined the need for more active support of effective management-worker communication and dispute resolution mechanisms, including the establishment of unions. We believe it is not our place, as a business partner, to become directly involved in promoting workers' elections and association formation in our suppliers' factories. Nonetheless, we understand the important role that unions can play in giving workers a voice and providing training and education on worker rights and workplace safety. While conscious of these benefits

of FOA, we are also aware that it is a contentious issue in many of the countries where our suppliers are based. Consequently, this re-statement of our position has resulted in a focus on:

- Gaining greater understanding of the local legal and political environment for FOA in each of the countries where our suppliers operate
- Developing individual country strategies for promoting management-worker-union collaborations that will resolve workplace issues and problems in a sustainable manner.

For details about promoting FOA in El Salvador and other countries, see the case study on page 35.

Revising our approach to compliance enforcement After canvassing the views of adidas-Salomon operations and factory management, we have refined the guidelines on enforcement and sanctions so that they offer a prioritised range of options rather than a policy of 'penalties and punishments':

- Identifying root causes of non-compliance
- Assessing supplier management attitude, capacity and level of cooperation
- Considering the needs of workers
- Involving a third party to assist with remediation
- Restating those areas considered 'zero tolerance'
- Explaining the interim steps which adidas-Salomon might take to respond to lack of performance.

These guidelines better reflect our 'partnering not policing' strategy, and will be communicated to our suppliers in the first quarter of 2004.

AUDITING COMPLIANCE WITH OUR STANDARDS /// In 2003 we took a critical look at our compliance work to ensure we were staying focused on our ultimate goal of self-governance for our suppliers. Some things have been working well:

- Auditing compliance performance and monitoring the subsequent remediation has defined supplier ratings against standards
- Training and capacity building have increased SOE awareness
- Our team has gained more experience in monitoring, and a broader exposure to diverse levels of compliance with workplace standards.

We also saw what is not working well in our compliance practices:

- Too few suppliers have internalised compliance programmes
- Too few suppliers have a strategic plan for compliance or management systems underpinning their compliance performance
- Our coverage of factories is still broad, and not deep enough
- Our auditing tools need to be more diagnostic
- The rating against labour standards is difficult to quantify and remains subjective.

Our activities in 2003 showed us that while effective compliance means gaining an understanding of local conditions and the compliance landscape, sustainable compliance means developing tools that support supplier ownership of compliance practice.

Auditing coverage At the outset of 2003 we reviewed how best to use available resources to strengthen labour and HSE compliance in the main factories. A simple risk management tool was devised and a ranking given to all Tier 1 suppliers. Those deemed to be 'high risk' were targeted for full rating audits or follow-up visits. Given their operating size, all footwear factories were added to this list, as were selected apparel, accessories and gear, and golf club production facilities.

Tier 2 suppliers continued to be a lower priority for the SEA team. Audit coverage has been ad hoc, and we have audited only a few selected material suppliers and other key subcontractors. However, to extend the reach of our programme we have incorporated the SOE requirements into our corporate product materials policy, and Tier 1 suppliers will also have to keep a record of their efforts to communicate the SOE requirements to their material suppliers and other service providers.

Monitoring and verification In 2003, there were 13 external, independent monitoring visits by FLA-accredited monitors. They included three audits in the Americas and 10 in Asia (see www.fla.org for more information). In late 2003, the FLA commenced verification activities for remediation plans that had been developed following monitoring visits in 2002.

There were 906 auditing visits by the SEA team in 2003. This included 162 in the Americas, 542 in Asia and 202 in Europe. There was increased attention to local market suppliers and to pre-production audits for supply chain candidates. This follows a formal procedure, agreed during the year, that sourcing staff will not place orders with new suppliers until a member of the SEA team has visited the factory to check on workplace conditions. Based on these pre-production visits, 77 were approved and 14 suppliers were rejected, on the basis that they would not be capable of complying with our SOE. Internal monitoring for 2003 increasingly focused on training and capacity building for suppliers and their staff (see pages 26-27).

New scoring scheme New and upgraded HSE and labour audit tools were rolled out in the first half of 2003, intended to improve the global consistency of compliance ratings and remedial action plans. While they achieved this and delivered a more comprehensive evaluation of supplier performance, they were found to be unwieldy – too lengthy to fill out within the time constraints of field teams covering hundreds of factories in the course of a year. More importantly, they did not adequately address the efficiencies of HR and HSE systems, the expertise of systems administrators, management commitment and a supplier's SOE strategy. These are all critical elements of our strategic approach to auditing.

Because of these limitations, we have reverted to the original five-star scoring scheme for this year's data (see page 32). However, we did find that the new tool has the potential to be used by suppliers themselves, as a checklist for assessing their factory compliance performance and progress on action plans. In 2004 we will be promoting this tool for the purposes of self-monitoring, and will continue to develop an audit-scoring tool for the SEA team that accurately evaluates management commitment, systems, SOE strategies and performance.

Audit Coverage 2003

Region	Number of active suppliers not audited yet	Number of suppliers audited in 2003 but removed from 'active' supplier list	Number of rejected factories after pre-approval audit
Asia	126	21	9
Americas	87	5	3
Europe	40	23	2
Total Global	253	49	14

Number of audits and training

Year	Audits	Trainings
2001	839	267
2002	1148 ¹	255
2003	906 ¹	206

¹ Excluding FLA audits (includes multiple visits in the same factory)

Independent audits¹

1st FLA Year	August 2001 – December 2002	42 Audits ²
2nd FLA Year	January 2003 – December 2003	13 Audits

¹ As part of the FLA membership

² First half of FLA year – 17 audits, second half – 25 audits

PROMOTING MANAGEMENT SYSTEMS /// Good management systems help our suppliers improve their day-to-day operations, bringing us closer to achieving our goal of supplier self-governance. We therefore encourage our business partners to establish systems and seek certification to international standards such as the OHSAS 18001 health and safety management, and the ISO 14001 environmental management system.

By rising to the challenge of establishing a certified management system, our suppliers are demonstrating that they have the commitment and personnel to continuously improve their performance. A database of appropriate consultants and certification bodies will be available in 2004.

Integrating health and safety standards into new manufacturing sites A number of our business partners are building new manufacturing facilities. At the design stage it is possible to eliminate potential Occupational Health and Safety (OHS) problems, effectively preventing them from ever entering the workplace.

The responsibility for safe design falls on a wide range of parties, including architects, business partner management and contractors. To help our suppliers we have drafted a guide to building a new factory. It promotes a holistic and systematic way to think about buildings over their entire life cycle.

Synergies with Lean Lean Manufacturing was first introduced to our footwear partner factories in 2001 and since then has been expanded to include all international apparel and accessories and gear suppliers, as well as our major material and component suppliers. The programme – run by a Continuous Improvement team (CI) within Global Operations – has proved valuable in helping our partners to shorten lead-times, improve product quality and reduce costs. In 2003 the CI and SEA teams collaborated on a number of initiatives:

- SEA 'Lean Champions' were assigned for each region – Asia, the Americas and Europe – to help integrate SOE requirements into Lean.
- SEA compliance staff have teamed with CI to complete joint factory audits in Thailand, China and Turkey. In the Americas, the regional SEA and CI teams collaborate on follow-up visits to factories in Mexico, Brazil and Central America.
- Consultants carried out an ergonomics assessment of two factories in Indonesia, and suggested ways to improve the arrangement of workstation and production layout areas and how equipment is operated.
- We conducted a survey of workers in two factories that had implemented Lean. Feedback indicated that suppliers needed to pay greater attention to: collecting and analysing performance data on turnover, sick leave, injury rates and productivity; developing wage structures that reward workers for productivity gains; and the effects on health and safety of new work patterns.

PROVIDING TRAINING AND GUIDANCE /// Training and education was the primary focus for 2003 and despite travel limitations, the SEA team still managed to conduct 206 training sessions for suppliers throughout the year. The training subjects were diverse, but fell into two broad categories: Back to Basics and Environmental Best Practice (EBP).

Back to Basics addressed basic CSR concepts, health and safety risk and hazard identification, and management-worker communication tools. Where feasible, the training took place at factory sites and included top management, production supervisors, worker representatives and internal adidas-Salomon staff responsible for operations on-site. The EBP training supported the launch of the Environmental Best Practice Guidelines and was aimed at factory SOE coordinators and environmental officers (see page 39).

Our formal Guidelines (covering employment, HSE and Environmental Best Practice) have been supplemented by an additional guideline on Fire Safety. We also issued several guidance notes on issues as diverse as the use of chemical spot-removers in apparel factories, to the banning of physical searches (or 'pat-downs') of the workforce as they enter and leave the factory.

Training in 2003 divided by region and type

Region	Type and number of training				Trainings in total
	General SOE training	Specific labour training	Specific HSE training	Environmental training	
Americas	20	16	4	0	40
Asia	31	25	20	9	85
Europe	61	9	10	1	81
Total Global	112	50	34	10	206

- General SOE training: e.g. practical on-site training; presentations for awareness raising.
- Specific labour training: e.g. worker-management communication; sharing best practice; freedom of association; factory overtime system; grievance and appeal systems.
- Specific HSE training: e.g. sharing best practice; chemicals in production.
- Environmental training: e.g. hazardous waste treatment; resources management; environmental best practice.

Number of business relationship terminations due to SOE problems in 2003

Region	Country	No. of terminations per country	Reasons for termination/SOE problems	Total no. of terminations per region
Asia	China	1	Poor HSE conditions, evidence of misleading and dishonest practices and interference with interview process, excessive overtime, incorrect payment of wages and benefits	1
Americas	El Salvador	1	Improper environmental and health and safety conditions	2
	Brazil	1	Discrimination, harassment, improper health and safety conditions	
Europe	Turkey	1	Incorrect payment of wages and benefits, excessive overtime, improper social security system	1
Global				4

Notes to table overleaf: Number of factories audited in 2003

The tables on pages 28-29 represent the efforts we have made to audit our supply chain. The table is divided into two categories – main factories and subcontractors – and split by product: apparel, footwear and hardware. The table compares active factories (status as of December 31, 2003) we audited in 2003 to the total number of supplier factories operating in that country, grouping the countries into our three regions: Asia, the Americas and Europe*.

* To reflect the way our SEA teams audit our suppliers, we include South Africa, Egypt, Tunisia, Morocco, Israel, and Syria under Europe in all the tables. For the same reason, Australia and New Zealand are included under Asia.

Number of factories audited in 2003

			APPAREL				HARDWARE ¹				FOOTWEAR			
Country	Total number of factories	Number of audited factories	Main factories		Subcontractors		Main factories		Subcontractors		Main factories		Subcontractors	
			Total	Number audited	Total	Number audited	Total	Number audited	Total	Number audited	Total	Number audited	Total	Number audited
Australia	12	3	11	3			1							
Cambodia	4	4	4	4										
China	164	61	87	31			66	19			11	11		
Hong Kong	10	1	4	1			6							
India	18	7	11	5			6	2			1			
Indonesia	32	32	21	21			8	8			3	3		
Japan	57	2	31	2	6		18		1		1			
Korea	83	18	68	9			14	8			1	1		
Lao P.D.R.	2	2	2	2										
Macau	1	0	1											
Malaysia	17	12	15	11			2	1						
New Zealand	9	3	8	3			1							
Pakistan	5	3	2				3	3						
Philippines	19	13	16	11			2	2			1			
Singapore	7	6	4	3	3	3								
Sri Lanka	3	0	1				2							
Taiwan	40	5	18	2			22	3						
Thailand	28	16	23	14			3	1			2	1		
Vietnam	28	20	15	9	1		5	4			7	7		
Total Asia	539	208	342	131	10	3	159	51	1	0	27	23	0	0
Argentina	15	5	12	5	1		2							
Brazil	37	17	11	11	5		1				9	6	11	
Canada	21	5	15	4	2		4	1						
Chile	2	1	1				1	1						
Colombia	4	1	4	1										
Costa Rica	1	0	0				1							
El Salvador	4	4	1	1	3	3								
Guatemala	3	2	2	1	1	1								
Honduras	3	3	2	2	1	1								
Mexico	28	21	12	10	15	10	1	1						
Peru	5	0	4				1							
Uruguay	1	0	1											
USA	59	4	18	1	11	1	29	2	1					
Total Americas	183	63	83	36	39	16	40	5	1	0	9	6	11	0

¹ Accessories and gear

			APPAREL				HARDWARE ¹				FOOTWEAR			
Country	Total number of factories	Number of audited factories	Main factories		Subcontractors		Main factories		Subcontractors		Main factories		Subcontractors	
			Total	Number audited	Total	Number audited	Total	Number audited	Total	Number audited	Total	Number audited	Total	Number audited
Albania	2	2			2	2								
Austria	2	0	1				1							
Bosnia	1	1											1	1
Bulgaria	6	6	3	3	3	3								
Croatia	1	1											1	1
Czech Rep.	1	0					1							
Egypt	1	0	1											
Estonia	2	0	1		1									
Finland	1	0	1											
France	6	0	1				5							
Germany	5	0	1				3				1			
Greece	6	2	6	2										
Hungary	1	0					1							
Ireland	1	0	1											
Israel	1	0	1											
Italy	24	3	17				6	3			1			
Latvia	2	0	2											
Lithuania	1	0	1											
Macedonia	3	3			3	3								
Morocco	2	1	2	1										
Norway	1	0	1											
Poland	1	0					1							
Portugal	32	15	13	8	19	7								
Romania	11	6	2	2			9	4						
Russia	3	1	3	1										
Slovenia	1	0	1											
South Africa	23	4	19	4			3				1			
Spain	2	0	1				1							
Sweden	2	0	2											
Switzerland	1	0	1											
Syria	3	0	1		2									
Tunisia	10	0	4		6									
Turkey	20	16	12	10	8	6								
UK	3	1	3	1										
Ukraine	2	2					2	2						
Total Europe	184	64	102	32	44	21	33	9	0	0	3	0	2	2
Total Asia	539	208	342	131	10	3	159	51	1	0	27	23	0	0
Total Europe	184	64	102	32	44	21	33	9	0	0	3	0	2	2
Total Americas	183	63	83	36	39	16	40	5	1	0	9	6	11	0
Total Global	906	335	527	199	93	40	232	65	2	0	39	29	13	2

¹ Accessories and gear

In 2003, 335 international and local suppliers were audited, as compared to 460 in 2002

In 2003, 37 percent of our suppliers' factories were audited. The coverage achieved reflects the following:

- Factory audits carried out by subsidiaries on behalf of the SEA team have not been included in the table
- We concentrated on auditing high-risk factories and facilities with a large order volume
- Factories with no order in 2003 may not have been visited.

EMPLOYMENT, HEALTH AND SAFETY /// In previous years we have reported on employment standards and health and safety in separate chapters. However, our programmes are now very closely linked, so we will report on them as two aspects of the 'workplace conditions' issue.

The SARS (Severe Acute Respiratory Syndrome) outbreak meant that 2003 was a difficult year for implementing labour and health and safety projects in Asia, the region where most of our suppliers' factories are located. In some cases, on-site visits and meetings had to be postponed or cancelled.

However, we made use of this period to research various projects, revise and develop new guidelines, and prepare the training workshops that were rolled out in the second half of 2003. We enhanced communications with Asian suppliers translating the Guidelines for Employment and Environmental Best Practice into other major languages, such as Chinese. We also revised and condensed the Fire Safety Guidelines into a more user-friendly document.

RESPONDING TO SARS /// We knew very little about SARS when the outbreak began. To help both our staff and our suppliers' employees, we reviewed guidance from the World Health Organisation and US National Centre for Infectious Diseases, and consulted local health organisations and other international companies. We issued advice to all our suppliers covering both preventative measures and contingency plans should a case of SARS occur. We stayed in regular contact with our suppliers to pass on any new information.

Our suppliers took a number of steps including:

- Establishing teams to manage and monitor SARS in the area
- Promoting personal hygiene with additional hand washing stations, and disinfectant units
- Measuring the body temperature of employees and restricting visitors to factories.

Due in large part to these measures, our suppliers reported no cases of SARS.

HEALTH AND SAFETY PERFORMANCE AT OUR OWN SITES ///

We encourage all our facilities to implement health and safety systems, and have produced guidelines to help them. We recognise that although infrastructure may vary significantly between different countries, the way we implement systems in our own factories can provide an example of best practice for our suppliers. Below we detail the health and safety performance of some of the sites we manage.

Scheinfeld, Germany After being awarded first prize in 2000 by the German Textile and Leather Trade Association for its advanced HSE system, the Scheinfeld footwear factory has continued to maintain a high level of occupational health and safety. The occurrence of only two minor accidents among 121 employees in 2003 is a measure of how well we have done.

Since 2000, each manufacturing-oriented workplace has been carefully reviewed for health and safety risks. As a result, precautionary measures have been developed and implemented. Further initiatives at this site in 2003 included:

- A free influenza inoculation for employees
- A transport shuttle service, which reduces vehicle emissions (see page 38), and reduces the possibility of accidents while employees drive to and from work.

Suzhou, China No industrial accidents were recorded at this apparel factory during 2002/2003.

Rumilly, France In 2003, an ergonomics programme to prevent occupational illness was initiated. The programme was offered to 40 technicians and to production subcontractors. During work breaks employees are encouraged to do a few minutes' stretching, using a regime recommended by a kinesiologist.

Workplace health and safety matters, and the gravity and frequency of workplace accidents, are recorded monthly and communicated to the staff via the intranet and in workshops. The number of reported accidents was reduced from 45 in 2002 to 34 in 2003. Additional fire drills were run during the year.

World of Sports, Germany At our headquarters, an administration facility with around 1,000 employees, occupational HSE management is integral to the manner in which the facility is managed. The HQ Works Council works closely with facility management and the HR department. Specific workplace HSE practices are co-ordinated by a professional health and safety officer and the company doctor. A number of occupational health and safety projects were conducted in 2003, some of which are ongoing:

- Evaluation of work place ergonomics, especially at computer work stations
- Ergonomics training for employees
- Measuring noise and illumination at work
- Special training and advice to employees about stress reduction, healthy living, and health measures during travel
- Analysing noise pollution and cases of skin irritation
- Evaluating emission measurements at workplaces
- Providing free influenza inoculation for all employees.

The company logbooks show there were only three accidents reported on the way to or from work, two minor work-related accidents, and none from sport activities on company grounds.

Health and safety in our Asian offices In 2003, the SEA team helped human resources and office management staff in our Asia offices to fulfil legal obligations regarding office safety, and also provided guidance and support during the SARS outbreak. In particular, the SEA team:

- Supervised evacuation procedures and specific fire drill training in offices in Indonesia, Singapore, Hong Kong, Vietnam and China
- Provided information and training to HR and office managers in the sourcing and operations office in Guangzhou, China, on how to conduct an HSE office inspection. This pilot will be rolled out to all sourcing offices in the Asia region in 2004.

In 2002, the Guangzhou liaison office established an Employees Committee. During 2003 elected staff representatives met regularly with management to review staff issues. Initially the Committee dealt with matters such as office perks (e.g. the staff allowance for adidas products) and office transportation. Over the course of the year, more challenging matters were discussed – such as the co-location of staff in factories and private insurance provision.

In 2004, the SEA team will work with the Committee to become more involved in reviewing office safety and ergonomics issues. While the purpose of the Committee was to improve communications between adidas management and staff, the Committee elections and meeting mechanisms are teaching local staff core skills in negotiation, committee conduct and workplace democracy. Similar committees will be established in other adidas-Salomon offices, taking into account local conditions and the needs of staff and management in those locations.

CASE STUDY

“The audit showed us the challenges we are facing which we were not aware of before.” Factory Management

Occupational Health Project China

To help us identify the occupational health hazards in our business partners' facilities, we engaged experts from a professional medical service provider. This project started with three pilot occupational health audits in China in 2003.

The consultants from International SOS Committee helped us better evaluate specific occupational health hazards and develop a strategy for long-term monitoring, tracking of injury and disease, and remediation of workplace hazards.

Ongoing occupational health training for factory doctors will be provided in 2004, as well as medical surveillance. Ultimately, the occupational health specialists will produce general guidance on occupational health management for our business partners.



SUPPLIER SCORING SYSTEM ///

Each year we audit our suppliers against our SOE principles and guidelines. We had hoped to use a new and upgraded auditing tool for this year's reporting. However, unforeseen difficulties with this tool meant we had to revert to our original five-star scoring scheme (see page 25 for details).

The following table summarises the performance of our suppliers against our SOE in 2003, using the scoring system described below. It reflects the lowest rating of either the HSE or labour performance of each supplier. Once a factory has been scored, an action plan is written.

The five grades of our supplier scoring system are:

There are numerous severe non-compliance issues. The factory has been given notice that business will be terminated unless there is immediate improvement.

There are some non-compliance issues and the factory is responding to the action plan slowly or with reluctance. The factory is monitored regularly.

There are minor non-compliance issues, and the factory is responding to the action plan positively.

Generally there are no non-compliance issues, and there are some best practices in place, confirmed in documentation.

There are no non-compliance issues and all of the factory's management system and practices are in place, confirmed in documentation.

International and local active supplier factories: labour and HSE standards

APPAREL

Labour/HSE standards	Asia	Americas	Europe
*	14	0	1
**	106	14	17
***	120	57	93
****	10	7	6
*****	0	0	0
Total active factories rated to date	250	78	117
Total rated in 2003	134	52	53
Total active factories in region	352	122	146

FOOTWEAR

Labour/HSE standards	Asia	Americas	Europe
*	1	0	0
**	7	7	0
***	14	0	4
****	3	0	0
*****	0	0	1
Total active factories rated to date	25	7	5
Total rated in 2003	23	6	2
Total active factories in region	27	20	5

HARDWARE¹

Labour/HSE standards	Asia	Americas	Europe
*	10	0	0
**	40	0	4
***	36	7	14
****	4	4	2
*****	0	0	2
Total active factories rated to date	90	11	22
Total rated in 2003	51	5	9
Total active factories in region	160	41	33

¹ Accessories and gear

TRAINING PROGRAMMES – FROM CAPACITY BUILDING TO SELF-GOVERNANCE ///

Before 2003, we anticipated that we would achieve 100% audit coverage of our suppliers' facilities each year. Given the limited resources of the team, our approach was one of 'fault-finding'; identifying HSE and labour non-compliances. This approach is not particularly effective in promoting occupational health and safety efforts, or in developing human resources systems, because often our suppliers do not have the technical knowledge to fully implement action plans and do not have access to important information sources.

Consequently, we face two major challenges:

- Helping suppliers develop skills and knowledge beyond basic compliance, and taking them nearer to self-governance
- Accessing information from government and other sources, given the complex technical, jurisdictional and cultural issues across the global supply chain.

As a result, it is critical to build capacity – to develop the right skills and knowledge base, and cultivate appropriate information sources – both internally within the SEA team and production and sourcing personnel, and externally with our business partners.

Internal capacity building – the SEA team SEA team members participated in a series of training exercises to increase knowledge. Some attended workshops on HR and management systems or participated in 'Train the Trainer' seminars. Some attended audit methodology training courses, for example those conducted by Social Accountability International, held in Asia and Europe. Others focused on enhancing their skills in occupational health and safety, and on-site risk and hazard identification.

Customised training sessions were also developed for the SEA team, covering:

- Changes in local legislation for countries where they work
- High performance work place systems – the link between sophisticated HR practices and the Lean production mode
- Strategic and social monitoring – a more holistic and comprehensive method for identifying root causes of workplace problems and non-compliance with the SOE.

In addition, SEA team members have participated in reviewing the strategy and tools for building sustainable compliance, and support methodologies for sourcing and operations programmes such as Lean.

Internal capacity building – sourcing personnel To improve and extend our production and sourcing personnel's knowledge of SOE, training workshops covering basic CSR concepts, and specific labour and health and safety issues, were held at international sourcing offices throughout the regions. Senior management and production staff from both adidas-Salomon and its business partners attended the one- to two-day workshops.

External capacity building – suppliers A number of different training workshops were delivered to our suppliers in the second half of 2003, including several capacity-building exercises for specific supplier groups within adidas-Salomon. For example, in February 2003 TaylorMade suppliers gathered in Humen, China to discuss the health and safety programmes, and identify staff training needs. Similar training sessions were held for other brands and their supply chains. The launch of the Guidelines on Environmental Best Practice provided another opportunity for factories to share best practice ideas and experiences.

CASE STUDY

"We very much hope that this project will help set a gold standard for other factory owners to follow." Marie Stopes International, Australia

Women's Health Project Vietnam

In 2002 we worked with the Hanoi-based Reproductive Health and Information Research Centre to develop materials on women's health issues for distribution to workers in Vietnamese factories.

Following 18 months of research and outreach with potential project partners, the framework for two major pilots in Vietnam was agreed and launched in the last quarter of 2003. The project partners, Marie Stopes International (MSI), Vietnam and the US Department of Labour-funded SMARTWork (Strategically Managing AIDS Responses Together), are working with key suppliers in the Ho Chi Minh City area. Both programmes evaluate:

- Factory management commitment to health issues
- Existing factory clinic services and worker needs in the areas of general reproductive health and HIV/AIDS.

MSI and SMARTWork project partners will develop in-factory training and services that address worker health in a sustainable manner. They will also identify and recommend treatment for workers whose medical needs are not being met adequately at factory clinics, or for whom access to medical treatment is not available.



EMPLOYMENT AND HEALTH AND SAFETY INITIATIVES ///

Fair Wage Study In our 2002 report we committed to publicly report on our work on fair wages and publish the findings of an independent study we commissioned in Indonesia. This we have done and the findings were presented at two forums in 2003: in Jakarta, Indonesia, and Columbia University in the USA. The findings have been posted on the FLA website: www.fairlabor.org/all/resources/livingwage.html

Based on the workshop dialogues and the Fair Wage Study research, we have defined a broad strategy to improve wages and benefits in our suppliers' factories. By 2006 we want each of our strategic business partners to have established a wage-setting mechanism that:

- Is transparent and has direct input from the workers – i.e. ideally through negotiation or collective bargaining
- Acknowledges and rewards workers for productivity gains
- Meets in full all legally mandated benefits
- Benchmarks basic pay at a level that is higher than the local minimum wage
- Includes and takes into account data on general cost of living and workers' needs
- Is part of a broader and much improved human resource management system
- Where practicable, promotes and supports the development of worker cooperatives.

To support these activities we have begun to assess the impact of reduced working hours, wage restructuring and the introduction of incentives and bonus schemes linked to productivity gains and Lean manufacturing. In 2004 for instance, we will use formulas developed by US NGOs in living wage studies to benchmark wage history in successful Lean factories in Honduras and El Salvador.

Working Hours project The SEA team formed a Working Hours Task Force to investigate the root causes of excessive working hours. The task force conducted interviews, surveys and a review of working hours data at selected Asia factory audits.

In the first year of the project, we found the causes of working hour problems in factories included: poor production planning, late material deliveries, worker retention, high turnover rates and seasonality. In the second year we focused on internal operations at adidas-Salomon that indirectly contribute to, and exert pressure on, our suppliers to extend working hours. In particular we analysed and assessed:

- adidas-Salomon sourcing, development and production systems
- adidas-Salomon customer (retail) expectations
- Performance of the nominated Tier 2 material suppliers.

The task force has submitted recommended actions to senior management in the following areas:

- A revised method of calculating T1 production capacity, order forecasting and unplanned orders, and capacity loading
- Suggestions for monitoring the quality and delivery performance of raw material suppliers
- Guidelines for last-minute order fulfilment demands and charges.

CASE STUDY

Freedom of Association El Salvador / Indonesia

Freedom of Association (FOA) is a particularly complex subject, with different legislation and practice applying in different countries. This requires us to be flexible, adapting our approach from country to country. Below are two examples of the ways in which we seek to promote compliance with the standard on FOA.

EL SALVADOR We teamed with compliance representatives from Reebok and four apparel suppliers, to engage Verité, a US based non-profit organisation, as trainers in Freedom of Association (FOA) and Collective Bargaining standards.

Four groups of 35 workers from each factory received four hours of presentation and mini workshops with Verité trainers. A fifth group, composed of managers from all factories, also received training. Verité selected the participating workers. Some were current and past participants in their factory's worker management communication committees.

The training materials included FOA and CBA (Collective Bargaining Agreement) legal precedents and case studies taken from the international and El Salvadoran labour codes, as well as the brands' own codes of conduct.

INDONESIA In 2003, we built on previous work with the International Labour Organisation (ILO). This included training workshops conducted for the management and officers of multiple unions in one of our supplier's factories to establish the rules for their collective bargaining negotiations. Other communication and problem-solving mechanisms have been explored through ILO training sessions, including the LMC (labour-management committee) concept.

LMCs provide a forum outside the legal mechanisms of the ILO conventions and Indonesian laws for worker representatives and management to debate and negotiate a range of issues, from workplace quality and productivity to workplace training. By focusing on production floor issues at the outset, the parties can begin to build trust in order to deal with the more complex social issues and workplace conditions and benefits.

In Indonesia, the social and political environment is dynamic. While workers may still experience problems exercising their right to FOA, nonetheless, larger numbers of workers now have the opportunity to participate in various forms of representation.

"We were afraid we would be lectured, but we've enjoyed this kind of participatory programme." El Salvadoran participant



ENVIRONMENTAL IMPACTS/// There are environmental impacts associated with our products at all stages of their life cycle, from product design to distribution. Our greatest environmental impacts occur at our suppliers' sites, where more than 95 percent of adidas-Salomon products are manufactured. We focus our activities on helping suppliers establish environmental management systems as the best way for them to reduce their environmental impacts. Using the environmental performance of our own production sites as examples of best practice, we develop appropriate guidelines and training programmes for our suppliers.

INTEGRATED PRODUCT POLICY /// The Integrated Product Policy (IPP) approach is increasingly seen as an effective way to address a product's environmental impact. It is based on the following key principles:

Life-Cycle Thinking IPP considers a product's life cycle, aiming to reduce its cumulative environmental impacts. It encourages measures to reduce environmental impacts at the point in the life cycle where they are likely to be most effective.

Marketability IPP acknowledges the fact that products need to perform and to be attractive in function, quality and price.

Stakeholder Involvement IPP aims to encourage all those who come into contact with the product (i.e. industry, consumers and government) to act within their sphere of influence and to encourage co-operation between stakeholders.

Continuous Improvement IPP aims for continuous improvements in environmental performance across the product's life cycle, whether in design, manufacture, use or disposal.

IPP footwear pilot study adidas-Salomon is exercising the IPP approach in a pilot study of athletic footwear products supported by the Environmental Ministry of Bavaria. Working with environmental consultancy INTECHNICA, the project covers all stages of the product's life cycle, from the extraction of natural resources, through to re-use or disposal.

The project's objectives are to:

- Develop methodologies, tools and systems to collect and disseminate information relevant to measuring the environmental impact of products
- Establish information systems that improve communication between the supply and distribution chains
- Develop and market a product that has been environmentally optimised, while remaining fully competitive in functionality, quality and price.

We have now completed the critical data collection phase, and the focus for 2004 will be the conceptual and strategic work.

The rest of this chapter follows the life cycle of our products – beginning with innovation and design development work. Following this we look at how we manage production impacts at our own sites, and then how we help our suppliers to reduce impacts at their sites. Finally we outline our efforts to reduce the impacts associated with distributing our products from factory to market.

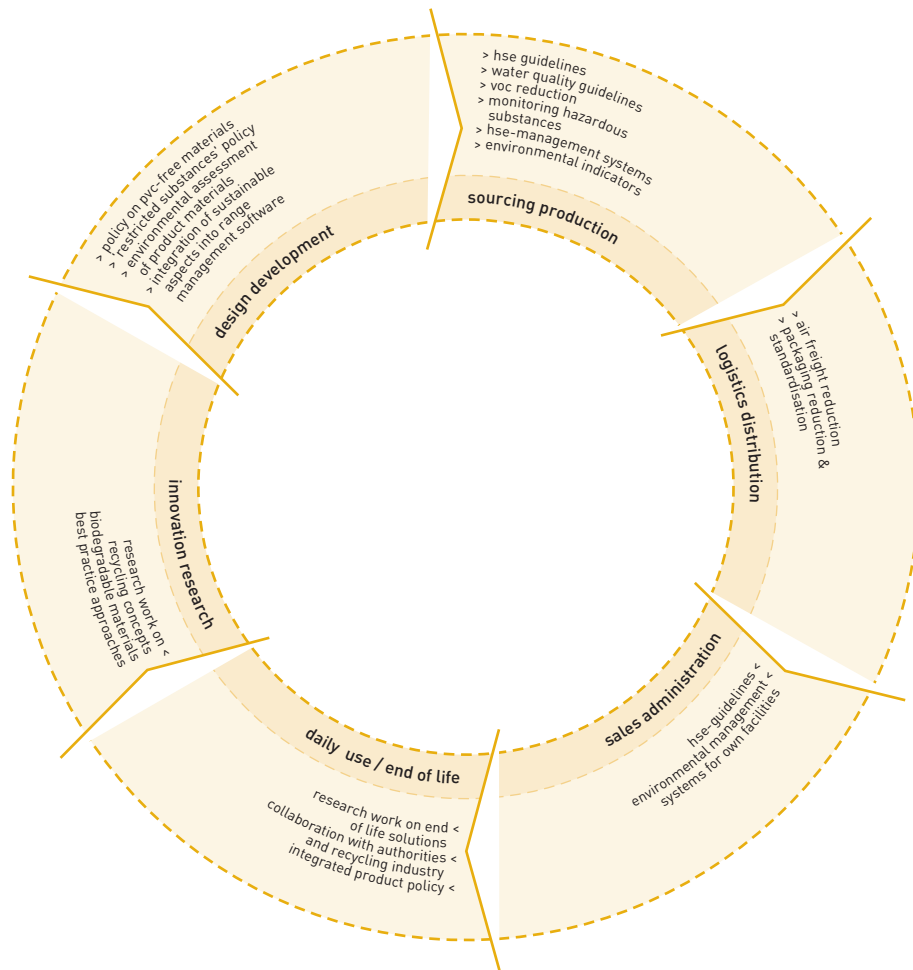
INNOVATION AND DESIGN /// Sustainability places challenging demands on our innovation and development teams. They need to balance a number of requirements: products not only have to be competitive, they need to be designed to be safe (during use and after disposal), and environmentally sound.

Reducing pollution with so-called end-of-pipe solutions offers only limited environmental benefits, so we strive to design out environmental problems. To this end we are exploring an increased use of reused and recycled materials.

Material selection policy To protect wildlife and help conserve the world's biodiversity, our policy is to not source raw materials from threatened or endangered species. If a proposed product material is derived from an animal on the red list of the International Union for Conservation of Nature and Natural Resources (IUCN), we will not use it.

Organic cotton strategy During 2003 we explored how we could use sustainable materials on a larger scale, especially organic cotton. Organic cotton is more expensive and will add to a product's price and as always, we have to strike a balance between environmental benefits and market issues. However, we remain committed to taking this project further. The target for 2004 is to finalise a product concept with the product management and development teams that includes sustainable materials and meets price and quality requirements.

Packaging materials Global supply and distribution requires well-packaged products, suitable for transportation over long distances, humid conditions and extreme temperature changes. The packaging itself serves as a promotional tool but nevertheless, we regularly check and optimise the volume and dimensions of product packaging, and strive to use recycled paper and other environmentally-friendly packaging materials.



Product life cycle

CONTROLLING AND MONITORING OF HAZARDOUS SUBSTANCES /// Hazardous substances are those that cause harm or are suspected of harming human health or the environment. Our policy is to control and monitor these substances; it is mandatory for all our sourcing business partners. The policy contains a comprehensive catalogue of restricted substances, and defines test methods, pre-treatments and health and safety limit values. These are based on both legal limits and recommendations by consumer organisations and other NGOs. The policy includes heavy metals, formaldehyde and ozone-depleting substances (CFCs), as well as a range of other chemicals. Material suppliers must prove that their materials comply with our standards by providing test reports from independent external test institutes on a regular basis. This is supplemented by random tests at production locations.

During 2003 the policy was updated and now covers all product categories and segments.

Eliminating PVC PVC materials are used in synthetic parts for shoes and sports shoes, and for technical hardware such as ski boots. After consulting stakeholders, and based on studies analysing the environmental impact of PVC, we adopted a policy in 2000 to eliminate PVC from our products where possible. This is because:

- PVCs contain a group of chemicals called phthalates, suspected of having long-term environmental effects and of causing cancer in animals
- Disposing of PVC is dangerous and costly: incinerating PVC creates hazardous waste such as hydrochloric acid, and some countries where our products are sold lack proper systems for removing PVC components.

We have made very good progress in finding substitutes for nearly all applications by using Polyurethane (PU), Ethyl Vinyl Acetate (EVA), Silicones and Thermoplastic Rubber, depending on the application. In 2003 adidas Footwear and Accessories and Gear nearly reached its target of being completely PVC-free. Some apparel styles from the international range, covering approximately 10 percent of all apparel units sold, still use plastisole inks containing PVC. However, we remain committed to seeking alternatives to the use of PVC in any of our products.

ENVIRONMENTAL MANAGEMENT AT OUR OWN SITES /// Most of our sourcing offices, sales subsidiaries and warehouses have insignificant environmental impacts compared to the environmental effects of manufacturing products in factories. adidas-Salomon operates eight production sites around the world. These factories comply with local laws and regulations, and have HSE activities that are managed by designated HSE coordinators. Corporate Guidelines for Health, Safety and Environment have been produced to support facility managers and HSE coordinators.

In 2003, there were no legal prosecutions reported for environmental liabilities at the Group's own sites.

Scheinfeld, Germany Since 1998, this footwear factory and training centre has been certified in accordance with the EU Environmental Management and Audit Scheme (EMAS). In 2001 the site was validated in accordance with EMAS II and in 2003 passed an annual environmental audit conducted by an external verifier. It will be revalidated in 2004 and an environmental statement will be published.

Scheinfeld also has a quality management system certified in accordance with ISO 9001:2000 which is reviewed annually.

Examples of 2003 environmental initiatives included:

- Installation of new roughing/gluing machinery that reduces the volume of adhesives applied by 50 percent. This has meant a further product VOC reduction of approximately four percent.
- An employee transportation shuttle service that saves the equivalent of approximately 580,000 km annually. This reduces the site's environmental impact by about 115 t CO₂, 320 Kg NO_x, 1.6 t CO, 160 kg soot and particles, and about 130 kg of organic compounds.

Suzhou, China adidas-Suzhou, part of our subsidiary in China, produces garments for the international and local market with 181 full-time and seven part-time workers. The factory was certified in accordance with ISO 14001 in 2002. The Production Manager, Plant Manager, Office Manager and Administration Supervisors are trained in SOE guidelines, and are qualified internal ISO 14001 auditors.

In 2004, this site will be re-audited by an independent environmental verification organisation.

Rumilly, France This factory has 950 employees producing skis and wheels for Salomon and Mavic. The factory has had a dedicated team addressing environmental issues since 1997, and in 2003, a new HSE group was formed to work with the service centre, human resources and medical staff on managing occupational risks, workplace safety and environmental issues.

The main achievements of the environmental programme in 2003 were:

- Internal environmental staff training of more than 300 employees
- Separation of used and polluted rags
- Commencement of polymer waste material separation
- Monitoring in-house treatment and handling of chemicals
- Reducing water consumption by 20 percent.

adidas-Salomon Headquarters 'World of Sports', Germany

The redesign of these old military barracks incorporated a number of initiatives that have reduced its environmental impact – including state of the art technologies to reduce energy and water consumption, and embedding the offices in the natural environment.

The general services and purchasing department follows Guidelines on Health, Safety and Environment, which involves:

- Ordering chlorine-free print and copy paper, recycled paper envelopes and cartons
- Collecting and recycling/refilling printer cartridges
- Using energy-saving printers and lighting.

HELPING OUR SUPPLIERS IMPROVE PERFORMANCE ///

Although we have limited control of the environmental impacts of the manufacturing process, we can influence how our suppliers act. We encourage our suppliers to manage their impacts and are developing tools so they can accurately record their environmental impacts.

Environmental indicators Since 2001, our major footwear business partners, producing 95 percent of our global shoe production, have provided data on their use of raw materials, energy and water, as well as solid waste and wastewater. A report documenting the study's findings and conclusions was distributed to the factories in 2003. It was clear that the factories understood the benefits of capturing and analysing data and we continue to promote the development of formal environmental management systems such as that implemented by Evervan in China (see page 40).

The indicators will be fine-tuned for application to our other business categories, e.g. Accessories & Gear. We will report back on progress in this area in 2004.

Environmental Best Practice Training In 2003 we used the Guidelines on Environmental Best Practice to deliver an environmental training programme for suppliers. The training was designed to:

- Raise suppliers' awareness of environmental best practice
- Provide a forum for suppliers to review, discuss and learn best practice from each other
- Help suppliers establish environmental management systems as the basis for continuous improvement.

The programme featured practical examples of environmental initiatives benefiting factory operations, such as energy and waste reduction measures.

A total of 55 key suppliers from nine Asian countries and 14 suppliers from seven European countries attended the 2003 training, with a broader global roll-out of the programme scheduled for early 2004.

Environmental Management Systems We actively encourage our suppliers to establish formal HSE and quality management systems as a way of better managing their operations. In 2003, 15 apparel factories producing for the export market were certified for ISO 9001, ISO 9002 and SA8000. The table shows the number of Asian footwear suppliers certified.

Certificates obtained by footwear supplier sites in Asia

Country	No of suppliers	IS 9001/2	ISO 14001	OHSAS 18001
Vietnam	7	3	3	2
China	11	7	1	0
Korea	1	1	1	1
Indonesia	3	1	0	0

CASE STUDY

Evervan China

The Evervan site in China – one of our major footwear suppliers – passed ISO 14001 certification in October 2003. Notable initiatives during the year included:

- Improved emission, dust and noise control in work areas
- Construction of a waste water treatment plant
- 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-conversation project.

The energy-saving project underlines the economic benefits of environmental initiatives. Compressors were fitted with energy-saving devices that reduced monthly energy use by 15 percent. Similar devices were also mounted on energy-intensive mixers and rubber mills, reducing that equipment's energy use by 21 percent. Payback on both investment applications will be realised within two years.

Recycled steam from the rubber room boiler now provides energy for cooking and hot water generation, and saves five tonnes of diesel fuel per month. The timeframes for investment payback on these two retrofits are five and three months respectively. Finally, recycling the condensed steam saves 814 tonnes of water and 15.1 tonnes of diesel fuel per month, with the return on investment achieved in 30 days.

Evervan reports the following figures:

- Saved water: 23.8 percent [ml³/pair/month]
- Saved electrical power: 2.68 percent [kwh/pair/month]
- Saved diesel oil: 42.5 percent [kg/pair/month]
- Saved gas: 47.6 percent [kg/pair/month]
- Ratio of reused waste material: 47.6 percent

“As a result of the implementation of the Environmental Management System and promotion of best environmental practice in our factory, we have saved a lot of money, especially in the area of energy consumption.” Factory Management



Freight types used to ship adidas products¹

% of product shipped	2003	2002	2001
FOOTWEAR			
Truck	4	4	3
Sea freight	95	94	96
Air freight	1	2	1
Sea and air freight	0	0	0

APPAREL

Truck	27	32	32
Sea freight	66	62	64
Air freight	6	5	4
Sea and air freight	1	1	0

HARDWARE²

Truck	6	7	5
Sea freight	91	86	92
Air freight	3	7	3
Sea and air freight	0	0	0

¹ Freight types used to ship expressed adidas products as a percentage of the total number of products transported

² Accessories and gear

Reducing VOCs in footwear factories Volatile organic compounds (VOCs) are found in solvents used to dissolve layering products in the manufacturing process, such as paints, cements, cleaners and inks. Toxicity varies with the type of VOCs but they can all cause breathing difficulties as well as other health complaints.

adidas-Salomon's policy is to reduce the amount of solvents used while also improving productivity and quality. Starting from a level of 140 grams/pair at the end of 1999, our Asian footwear suppliers committed to reaching a level of 20 grams/pair in 2003 for adidas-products.

Our suppliers achieved an average figure of 24 grams/pair in 2003 (see chart) by using water-based alternatives in primers and adhesives, and extending the use of hot melt systems. This level is below the 2007 European standard of 25 grams/pair.

We did learn that the calculation for measuring levels in Salomon products used a faulty methodology. We reported that the VOC content was 60 grams/pair in 2002 but in fact the figure was 130 grams/pair. The figure at the end of 2003 is 80 grams/pair.

We remain committed to achieving our goal of 20 grams/pair for adidas footwear products and to further reducing VOC consumption for Salomon footwear. We have begun extending this initiative to other product areas such as Accessories and Gear. In the light of the Salomon error, we will be reviewing all previous VOC data and will report the findings in 2004.

ENVIRONMENTAL IMPACT OF PRODUCT TRANSPORTATION ///

The fuel used to transport our goods from the countries of origin to the selling markets creates carbon dioxide emissions – a major contributor to climate change. Our policy is to minimise the environmental impact in transporting our goods. Airfreight results in the greatest emissions of carbon dioxide, so we remain focused on reducing the airfreight component of our product transportation.

Most of our goods are transported as sea freight shipments, but products are shipped by air to accommodate serious production delays and time sensitive product launches. We met the 2001 figures in 2003, with the exception of apparel, which was in large part due to the serious logistical challenges caused by SARS (see table on page 40).

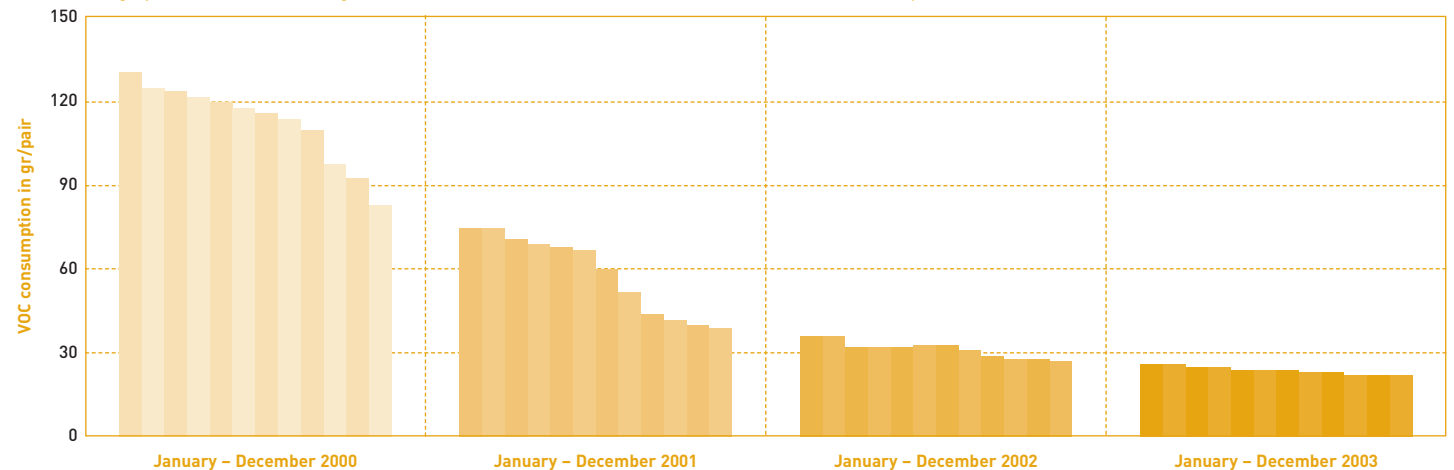
Carbon dioxide emissions are measured in grams carbon dioxide per kilometre each tonne travels (grams CO₂/km t):

- 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.

Source: German Environmental Protection Agency.

Reducing VOCs in footwear supply factories

The graph below shows an average obtained from our factories in China, Indonesia and Vietnam over four years.



COMMUNITY INVOLVEMENT /// Currently, our community involvement practice is decentralised, which means that our subsidiaries and group entities manage programmes and charitable donation activities at the country level. At adidas-Salomon headquarters in Germany we receive more than 2,900 enquiries a year from individuals, schools, teams, local and global organisations.

OUR CORPORATE STRATEGY /// In 2003, a Group-wide survey revealed the great range and variety of community engagement that takes place within our Group. The same survey, customised for our supply chain partners, showed similar diversity in the community activities of our business partners. We are using the results of these surveys to help us develop meaningful strategies on Corporate Giving, and on Community Involvement in our supply chain. Both strategies need to be complementary and based on our corporate values, but also need to be flexible enough to include the different aspects of local cultures and practices. Our aim was to complete these strategies in 2003, but this was not achieved.

We present here examples of Community Involvement activities within the adidas-Salomon Group, and the activities by our partners in the supply chain. The activities can be summarised as volunteerism, donations (both cash and in kind services), and community relations. Many of the activities support youth development, education, and health and sports programmes, but in general, all are focused on helping people perform at their best; to reach their full potential as individuals and members of their communities.

INTERNAL GROUP ACTIVITIES ///

Volunteerism In the United States, employee volunteering programmes at adidas America are aligned with corporate charitable giving and community relations strategies that support youth development, education and youth sport. The programme allows for voluntary work during working hours, at the discretion of individual managers. Employees are active volunteers with the Boys and Girls Club of America (see <http://www.bgclubportland.org/>), and other local groups.

In Europe employees can take part in adidas-supported community activities during working hours.

In Turkey, employees from our Sourcing Liaison Office volunteer on a joint project with the Friends of Children foundation. The group provides ongoing support for 40 children who are victims of the recent earthquakes in Turkey.

Furthermore they support the Child Protection Agency (Sirinevler branch) and 250 children, with cash and non-cash donations for basic needs such as education, living quarters, and food.

Donations In Vietnam, employees from the adidas Sourcing Liaison Office and factory partners support the Saigon Children's Charity. Nearly 100 underprivileged school-aged youth in and around Ho Chi Minh City receive scholarships covering annual tuition fees, uniforms, and books – as well as food, and cash payments. More details are available from www.saigonchildren.com/

At adidas-Salomon headquarters in Herzogenaurach, Germany, community groups in our home town and suburbs received a number of product donations. We are the official sponsor of the Franconian International School in Herzogenaurach, and financially support the Lebenshilfe, an institution that provides shelter, workshops, and organised activities for children and young people with disabilities.

On the international level, we sponsor several international organisations, including SOS children's villages, UNICEF and Right to Play (formerly known as 'Olympic Aid'). These groups support children in refugee camps and poor communities through the development of sport and health programmes.

Community relations In the United States, adidas America supports urban renewal in North Portland, home to our new North American Headquarters. We have taken an active role in building relationships and partnerships with local business and civic organisations that are instrumental in the area's urban development projects.

In Vietnam, employees from the adidas Sourcing Liaison Office and a supply chain partner support the Christina Noble Foundation with product donations to underprivileged youth in their sports programme. More information is available from www.cncf.org

EXTERNAL SUPPLY CHAIN /// Globally, our business partners contribute actively to their local communities in many different ways: by donating blood to the Red Cross, donating cash to help local children attend school, and/or scholarship schemes and fundraising for local schools, hospitals and other organisations. They also provide food and clothing to local disadvantaged families, and help with local environmental projects, such as tree planting and public park cleanups. Some examples follow:

Volunteerism A volunteer group of factory workers from one of our suppliers in China is joining a community project to clean up the local area on World Environment Day, June 5.

Donations A supplier in Indonesia has created a foundation through which it supports workers and their families with educational, medical and other needs.

In Turkey, one of our suppliers runs an association that makes cash and non-cash donations to students and families in need. It has also made a donation to an elementary school, to develop 30 classrooms including a computer room.

The management team of a supplier in El Salvador donates mechanical equipment to an organisation that provides vocational training for people with disabilities; and hires workers trained by the organisation.

Community Relations A Bulgarian supplier has helped establish a programme called 'Together in Sports for a Better Quality of Life', which organises sporting events for the local community.

NEXT STEPS /// We will continue to work on the development of a formal corporate policy for charitable donations and corporate giving. We will continue to research ways to support our suppliers' community involvement efforts and so maximise the Group's corporate philanthropy efforts. Our goal in 2004 is to re-survey selected group entities and suppliers so we better understand their initiatives for community involvement and their criteria for choosing beneficiaries. We will report on that in next year's report.

CASE STUDY

The Salomon Foundation

For a long time, mountain professionals and snow racers have helped Salomon to improve sport equipment and to facilitate sport practices for users. To thank them for their contribution, Salomon S.A. and the Salomon family established the Salomon Foundation in March 1999. The mission of the foundation is to support mountain professionals and their families in cases of accident, illness or death. Beneficiaries are high-altitude mountain guides, ski and climbing instructors, ski patrol members and first-aid workers, mid-altitude mountain guides and snow racers (including people with disabilities).

Although mostly funded by the Salomon family, the Salomon Foundation is run by the Foundation of France and is not part of Salomon itself. Individuals can apply for support directly to the administrative committee, or through their professional organisation. The Foundation gives on average 25 to 30 grants a year, totalling €80,000–100,000, and has the resources to operate at this level for the next three years.

More details are available from www.fondation-salomon.org/





review:

Amidst all the pressure to perform and meet stakeholders' expectations, it's vital to create space for analysis and reflection. Here we assess our progress against targets in 2003, and map out specific actions we will be taking as a result in 2004.

This section also helps you review the document itself. You can check it against Global Reporting Initiative guidelines for social and environmental reports; and refer to the glossary for our definition of terms.

THE JOURNEY ///

THE JOURNEY





The six inter-linked roads on the journey to sustainability and strong governance are shown below. The shaded runners show our performance starting in 2000 and ending with 2003. Please refer to the key.

PROGRESS AGAINST TARGETS

Progress against targets on page 47–48 summarises all the targets we set for 2003. We estimate how much of each target we have met, make any relevant notes, and refer to the page or pages in this report where you can find more detailed information about the topic.













TARGETS FOR 2004

Our targets for 2004 are listed on page 49.











Key			
			
2000	2001	2002	2003



PROGRESS AGAINST TARGETS ///

Targets for 2003	Actual performance	0	10	20	30	40	50	60	70	80	90	100%
ENVIRONMENT												
To reduce VOC-solvent levels to below 25 grams per pair of shoes.	Overall, solvent consumption was reduced to 24 grams per pair of adidas footwear. The method that was used for measurement of solvent consumption for Salomon footwear in 2002 was faulty and had to be revised. However, a 30 percent reduction of solvent consumption for Salomon products was achieved.											
To reduce further the use of hazardous chemicals in hardware manufacturing in accordance with international standards.	We increased the use of water based-cementing and printing technologies in accessories & gear products. Metrics have been developed to measure and report VOC-consumption for certain hardware product categories, but an average VOC figure cannot be reported because of the wide variety of products.											
To provide a progress report about improved measurement of environmental impact.	The environmental impact of footwear production facilities in Asia and Europe (accounting for more than 95 percent of international footwear production) was recorded. Results were analysed and footwear factories were provided with individual status reports highlighting potentials for improvements. The reports also indicate that data quality and accuracy need to be improved.											
To develop a strategy to extend the use of organically grown cotton for apparel products.	Market research was undertaken to identify possible options for the use of organic cotton in apparel products. Due to limited applicability and price restrictions, the research focus has been extended beyond organic cotton to review other sustainable material concepts.											
To provide a progress report about the pilot project and case study on principles of integrated product policy.	Following the IPP principles, a 'Product Panel' representing all decision-makers has been established. Quantitative data indicating the environmental impact of the sample's life cycle was generated. Improvement potentials have been submitted to innovation and design teams developing product prototypes.											
MANAGEMENT												
To provide 100 specific training sessions to build capacity in suppliers' factories.	In total 206 training sessions were held, of which 50 were training sessions on Employment Standards and HR systems, 34 were training on HSE standards and 10 on Environmental Best Practice.											
To further enhance the relationship to sourcing operations through system development and participation in key initiatives.	SOE-compliance has become an integral part of the supplier-pre-approval process and of the overall supplier performance rating. Licensee partners are being trained in applying the compliance programme with their suppliers. Social and HSE initiatives continue to be integrated with the Lean Manufacturing efficiency programme.											
To increase employee awareness of the Group's social and environmental programmes.	Various internal HR-sponsored awareness-raising sessions for new and current employees were held. adidas-Salomon brands and subsidiaries received SOE-orientation sessions. Employees have continuous access to updated SEA programme information through the website, intranet and global PR newsletter.											
To conduct regional stakeholder dialogues and focused group discussions in each region – the Americas, Asia and Europe.	Formal stakeholder dialogues were held in Europe and Asia, including worker stakeholder meetings in Turkey and Portugal. Some stakeholder meetings scheduled for Asia had to be postponed due to SARS. In the Americas, stakeholder dialogue focused on practical training with workers in El Salvador on Freedom of Association (FOA).											
COMMUNITY INVOLVEMENT												
To finalise and execute a corporate approach to fund and support community programmes.	A survey was conducted among subsidiaries and group entities to identify Community Involvement activities. The results indicate multiple sets of engagement in local communities that should be included in the framework of the corporate approach. A strategy has not been finalised.											
To survey suppliers in order to obtain an overview of the level of community involvement.	261 main suppliers have been surveyed globally. Results showed that almost all are involved in some form of Community Involvement, either through voluntary services or by providing cash or non-cash donations.											
To more effectively report on community involvement in 2003 report.	The report covers the research findings and details examples of corporate and supply chain initiatives.											

PROGRESS AGAINST TARGETS continued ///

Targets for 2003	Actual performance	0	10	20	30	40	50	60	70	80	90	100%
SUPPLIERS												
To ensure deeper coverage of higher risk factories based on the risk assessment generated across the supply chain over the previous two years auditing. Shift audit methodology from 100 percent annual coverage of supply base, to focused remediation, action plan development and follow-up, and training with fewer, but higher risk, factories.	We applied a risk assessment tool for scheduling monitoring in all three regions. Higher risk factories were prioritised and deeper coverage of a select few suppliers was achieved. Not all priority factories in Asia were fully audited, due to travel restrictions. Training and best practice workshops were held with suppliers.											
At least 12 factories in the supply chain to be audited by FLA independent monitors in 2003. Progress for remediation of these 12 factories and the 42 FLA audited factories (2002), will be monitored throughout 2003. The FLA will post tracking worksheets with selected audit findings and remediation results on its website in 2003.	13 factories were audited in 2003, 10 in Asia and three in the Americas. FLA site visits to verify factory implementation of action plans started in December 2003 and are ongoing. More than 10 adidas IEM reports from 2002 and 2003 are now posted on the FLA website (www.fairlabor.org).											
Fully use the computerised rating systems for factory audits and develop appropriate databases and analytical techniques to assess the results.	The computerised rating system was rolled out in 2003 across three regions. Following feedback, a more user-friendly version of the software was developed. A full set of annual ratings was prepared for Asian footwear factories and for other selected apparel and accessories and gear suppliers internationally. Data analysis, however, has been limited.											
Increase transparency through key projects and establishing benchmarks for collaborative projects with NGOs. Define metrics in the adidas-Salomon business model that indicate change and improvements in working conditions in the supply chain.	NGO partnerships include ongoing leadership in the FLA, collaboration with the Workers Rights Consortium and Marie Stopes International, and developing the work of the Fair Wage Study with US and Latin American NGOs. Improved supplier audit tools were introduced but do not meet our needs, and so will be revised in 2004.											
Complete the fair wages pilot study and run a multi-stakeholder workshop to discuss the findings.	The reports for the fair wage study were completed and peer reviewed by an independent specialist. The findings were presented at a multi-stakeholder meeting in Indonesia and in the United States. The results of the workshop and a summary of the findings of the pilot study have been posted on the FLA website.											
FINANCE												
Increase Group sales by around five percent.	Group sales reached €6.267 billion (currency-neutral sales up five percent).											
Deliver double-digit currency-neutral sales growth in Asia and North America.	Currency-neutral sales grew seven percent in Asia but declined six percent in North America.											
Deliver a gross margin of 42–43 percent.	Gross margin reached 44.9 percent.											
To deliver earnings growth at a higher rate than 2002.	Earnings went up 14 percent to highest EPS ever.											
Maintain and develop shareholder confidence.	Share price went up 10 percent and the shareholder base expanded (international shareholders now represent more than 80 percent of identified shareholders).											

TARGETS FOR 2004 ///

0 10 20 30 40 50 60 70 80 90 100%

ENVIRONMENT

- To keep consumption of VOC-levels close to 20 grams/pair of shoes; to include Salomon products in the VOC reporting framework
- To work with material suppliers to replace PVC plastisole prints and to use technically feasible material options for upcoming product styles
- To renew EMAS certification for the adidas-Salomon production site in Scheinfeld, Germany and to publish the environmental statement 2004
- To report on findings, progress and results of the 'Integrated Product Policy Study'
- To establish a monthly reporting system to measure the environmental impact of footwear suppliers' factories, based on an environmental indicators system field-tested in 2001/2002; to report on results; to extend the systems to main accessories & gear factories
- To report on a waste management study conducted with selected business partners
- To provide a progress report about the Group's efforts regarding the use of sustainable product materials.



MANAGEMENT

- To rework and launch the corporate code of ethics for adidas-Salomon employees globally
- To conduct formal stakeholder dialogues with selected target groups in Europe, the Americas and Asia
- To participate in an EC funded multi-stakeholder initiative to build capacity in the Bulgarian Apparel Industry
- To outline a corporate policy on HIV/Aids prevention and treatment of affected employees
- To launch programmes in selected factories that support activities by integrated SEA and Lean factory teams that improve workplace conditions and efficiencies, and worker participation.



COMMUNITY INVOLVEMENT

- To re-survey selected group entities and suppliers to better understand the diversity of community involvement and the criteria for selecting recipients. We will report on progress in next year's report.



SUPPLIERS

- To roll out the revised strategy of 'sustainable compliance': suppliers to establish effective HR and HSE management systems; OHSAS 18000 and ISO 14001 mandatory for strategic business partners by end of 2005
- To support suppliers in achieving sustainable compliance by conducting 100 specific training sessions focusing on human resources management, OHSAS 18000 and environmental best practice
- Field testing of revised audit technique and development of meaningful key performance indicators as basis for sourcing decisions
- To communicate the SOE policy for Tier 2 suppliers
- To roll out projects related to workers' health, in particular HIV/AIDS education and prevention
- Targets consistent to our obligations as a participating company in the FLA:
 - To complete the required Independent Monitoring activity for year 3
 - Participate in the launch of FLA value-added exercises
 - Finalise all other activities in anticipation of 2005 programme certification.



FINANCE

- Drive currency-neutral sales growth of three to five percent
- Deliver currency-neutral top-line growth at all brands
- Expand gross margin for the fifth consecutive year
- Visibly increase operating margin
- Drive earnings growth of at least 10 percent
- Further increase shareholder value for investors.



ABOUT THIS REPORT AND THE GRI ///

The guidelines of the Global Reporting Initiative (GRI) provide an internationally consistent format for social and environmental reports. While the GRI guidelines are a useful benchmark for report readers, they do not fully take into account the nature of the sporting goods industry, where the impacts of supply chain management outweigh the direct social and environmental impacts of the companies themselves.

For this reason, while we have followed the GRI format as much as is practical and helpful, this report goes outside the requirements of the guidelines in order to provide the range of information that is relevant to our business.

We acknowledge that there are still gaps in our reporting, and the GRI guidelines have proved helpful in identifying these. (To make the gaps clear to readers, we have highlighted them in the index to the right.) Some of this information is covered in our Annual Report, or on our website at www.adidas-Salomon.com

For more about the GRI and its reporting guidelines, visit www.globalreporting.org

GRI ELEMENT	REPORT SECTION OR INDICATOR	PAGE
Vision & Strategy		
1.1 Sustainable development vision and strategy	CEO statement Vision and Strategy	3 6-7
1.2 CEO statement	CEO statement	3
Profile		
2.1 Name of reporting organisation	Group profile	8
2.2 Major products, services and brands	Group profile	8
2.3 Operational structure	Corporate governance	11-12
2.4 Description of customer groups	Group profile	8
2.5 Location of adidas-Salomon operations	Group profile	8
2.6 Nature of ownership	Group profile	8
2.7 Nature of markets served	Group profile	8
2.8 Scale of reporting organisation	Group profile	8
2.9 List of adidas-Salomon stakeholders	Stakeholders	14
2.10 Contact person(s) for the report	Contact us	52
2.11 Reporting period	About this report	2
2.12 Date of previous report	About this report	2
2.13 Boundaries of the report	About the report and GRI	50
2.14 Significant changes in size, structure, ownership or products	Not applicable	
2.15 Basis for reporting on joint ventures	About this report Vision and Strategy Suppliers	2 6-7 18-20
2.16 Explanation of any re-statements of information in previous reports	Not applicable	
2.17 Decisions not to apply GRI principles	About the report and GRI	50
2.18 Criteria/definitions used	Not reported	
2.19 Significant changes in methods	Suppliers Improving the way we work with suppliers	18-20 24-29
2.20 Policies and practices on accuracy, completeness and reliability	Suppliers Improving the way we work with suppliers	18-20 24-29
2.21 Policy for independent assurance	CSR Network Statement	15
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3.3 Process for determining the expertise of Board members	Not reported	
3.4 Process for identification and management of risks	Corporate governance	11-12
3.5 Executive compensation and achievement of company goals	Not reported	
3.6 Organisational structure and key individuals for implementation and audit	Corporate governance Suppliers	11-12 18-20
3.7 Mission and values statements, internally developed codes	Standards of Engagement Vision and strategy Suppliers	21 6-7 18-20
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3.8 Mechanisms for shareholders to provide recommendations	Corporate governance	11-12
3.9 Identification and selection of major stakeholders	Stakeholders	13-17
3.10 Stakeholder consultation	CEO statement Stakeholders	3 13-17
3.11 & 3.12 Information from stakeholder consultation and its use	CEO statement Stakeholders	3 13-17
3.13 The precautionary principle	Not reported	
3.14 Voluntary charters or other initiatives	Stakeholders Throughout the report	13-17
3.15 Industry and business associations memberships	Corporate governance Stakeholders	11-12 13-17
3.16 & 3.17 Policies and systems for managing upstream and downstream impacts and approach to managing indirect impacts	Corporate governance Suppliers Our performance	11-12 18-20 24-43
3.18 Major decisions on operational changes	Improving the way we work with suppliers	24-29
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EN3 & EN4 Direct and indirect energy use	Environment ¹	36-41
EN5 Total water use	Environment ¹	36-41
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EN9 Ozone-depleting substances	Not reported	
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¹ We have referred to programmes in place to address these issues with our supply chain in the section indicated. Information on our own performance has not been reported or has been reported partially.

GLOSSARY ///

Annual Report Financial report including financial statements issued on an annual basis.

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.

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.

Dow Jones Sustainability Index Share index of companies that are considered leaders in the area of sustainable development and conduct their businesses accordingly.

Environmental Management System (EMS) 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 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.

Global Reporting Initiative (GRI) Independent global institution developing a generally accepted framework for sustainability reporting.

HSE Health, safety and environment.

Hot melt Environmentally safe bonding technology using heat-activated adhesives.

International Labour Organization (ILO) UN agency promoting social justice and human and labour rights.

ISO 14000/1 Environmental management standard.

Lean adidas-Salomon manufacturing efficiency programme designed to improve overall factory performance in terms of delivery, quality and cost.

Multi-Fibre Agreement (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 expires at the end of 2004.

Non-governmental organisations (NGOs) Special interest groups, often not-for-profit, raising awareness of sustainable development issues in business.

OHSAS 18000 Occupational health and safety standard.

Polyvinyl chloride (PVC) Synthetic material used in the manufacture of sports apparel and hardware that is being phased out in some products because of its adverse health and environmental impacts.

Social and Environmental Affairs (SEA) adidas-Salomon department responsible for producing and developing sustainability policies and initiatives, and promoting social and environmental awareness throughout the company and its supply chain. The key functions of the department are carried out by the SEA team.

Stakeholder Person, community or organisation that affects, or is affected by, the operations of a company. Stakeholders may be internal (for example, employees) or external (for example, customers, suppliers, shareholders and the local community).

Stakeholder dialogue Engaging in a structured way with all the people who have an interest in the company (stakeholders) in order to understand their concerns and respond appropriately.

Standards of Engagement (SOE) A set of labour, health and safety, and environmental principles designed as tools to help adidas-Salomon choose supply chain partners, monitor their performance and identify problems. The standards are derived from international legal precedence established by the ILO, United Nations and other regulatory agencies.

Sustainable development Development that meets the needs of the present without compromising the ability of future generations to meet their own needs.

Volatile Organic Compounds (VOCs) Solvents that can cause breathing and health problems. VOCs are by-products of the shoe manufacturing process.

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