

**adidas Group First Quarter 2012 Results**

**May 3, 2012**

**Q&A session**

**adidas Group participants:**

**Herbert Hainer, adidas Group CEO**

**Robin Stalker, adidas Group CFO**

**John-Paul O'Meara, Vice President Investor Relations**

**Andreas Inderst – Exane BNP Paribas**

**Good afternoon, gentlemen, and congratulations on the strong start to the year. My first question is on brand adidas, which is showing excellent momentum. You said your market share is now over 10% in North America and you also gained nice market shares in Europe. Can you share any market share targets, maybe for the next two years? And what are the biggest operational risks you see in the North American market and in the European market for brand adidas. And my second question is on India. I assume you have sales of significantly less than EUR 300 million in India, yet your one-off costs will be up to EUR 70 million. That's quite a lot. Maybe you can elaborate a little bit more on what you want to achieve there and maybe you can provide a phasing of the one-off costs expected through the year? And, related to that, what will be the EPS guidance, excluding your EUR 70 million one-off?**

**Herbert Hainer**

So let me start with the first one, market share in North America and Europe. Obviously, we haven't given out any market share targets, but there is no doubt that, especially in North America as I always have said, we have still a lot of potential. As you know, we are concentrating on building our business on a sustainable and solid platform with key pillars in basketball, in running, in training, in football, and, obviously now you see the first results. The same is true in Europe despite the economic challenges. Our results of plus 7% in the first quarter are quite exceptional and this will definitely continue as we now have the European Championships and the Olympics ahead of us.

So, overall, I just can confirm what you mentioned. We have extremely strong momentum with brand adidas and I definitely see it continuing, going forward.

Concerning India, I think you will understand that we have an on going investigation there and, therefore, we cannot comment on any of the individual items that you have asked about. We definitely believe that in three months from now when we host our second quarter call that we can give you more details on India.

**Andreas Inderst**

**And what's the guidance on EPS, excluding all your one-offs?**

**Robin Stalker**

Andreas, we've given you the guidance. We've clearly said what we think may be the one-off impact. At the moment, we can't quantify that any better. As Herbert said, without doubt we'll be in a better position to talk about this in the second quarter. We've taken the best estimate we have and we've given you the guidance on that basis.

**Andreas Inderst**

**Okay, good. Thank you.**

**Matthias Eifert – MainFirst Bank AG**

**My first question is on the Reebok gross margin improvement, was it purely an effect of shifting the NHL business to CCM? Or is it even up excluding that effect, as I would assume it has a lower gross margin?**

**Secondly, in North America, Wholesale sales were down 2%. Is that all driven by the Reebok toning effect and can you give us a bit more detail on that, because I want to understand how that fits together with your comment about the market share gains?**

**And lastly, can you give us a bit more detail on your strong growth in Style. Was that equally shared by the NEO label and Originals, or is there a big difference in terms of those growth rates?**

**Herbert Hainer**

So, we're really pleased with the underlying improvement or continuing improvement in the Reebok gross margin. There is definitely an underlying improvement and you are correct, it has been helped by the shift of the NHL product into CCM Hockey, though it's a fairly small amount. So there is definitely an underlying improvement and you can see that through the mix in the faster growth in the Retail segment with higher margins. So, that's continuing the way we want it to and we've closed the margin gap. I think the first quarter Reebok to adidas gap is now only about 8 percentage points.

In terms of the Wholesale business, yes this was impacted by the shift, but otherwise, I don't think there's anything material in that number.

**Robin Stalker**

And to answer your third question, Matthias, on Style - as you've been following us for quite some time, you have seen that over the last couple of years we were very successful in driving our Style business, mainly through Originals, and, once again, this is the big driver. Also, we are very happy with our NEO business, which is up 30% in the first quarter, but it is too small to have a big impact yet. So, it's still the underlying Original business, of course, coupled with NEO and the other Style variants, which are all growing.

**Matthias Eifert**

**Excellent. Thank you.**

**Jurgen Kolb – CA Cheuvreux**

**First of all, on Japan, I think you experienced a very nice rebound in the first quarter there. Just help us, again, on the drivers of that. Obviously, there was some kind of a jump from the tragic events there last year, but it should also have a very positive impact in the second quarter as I think your stores are now all open. So, the rebound in Japan should also materialise in Q2 and Q3, if I'm right here?**

**Secondly, on the input costs, again there is a very strong increase there. Any additional comments on whether this might now have peaked and you're expecting this pressure to ease in the coming quarters?**

**And then lastly, on Reebok, you mentioned a new product range to be launched next year. Is there also a new marketing campaign this year that you're planning to launch in order to give the brand additional support - maybe here specifically in Western Europe? Perhaps an update on your plans for Reebok for the first half of this year in Western Europe and also in the US? Thank you.**

**Herbert Hainer**

Okay, Jurgen, let me take the first and the third one and Robin will answer input costs. You know that we have a very strong business in Japan. We are the clear market leader and, as you have seen in 2011, our sales decreased by only 4% during the whole of the year. So, our business is quite solid and this is also reflected in the first quarter of this year. Sales in the second part of March were also solid, with the comparable store sales helping us a little bit. Overall it is because of our strong business in Japan, and this will definitely continue within the next quarter and during the second half of the year.

On your third question on Reebok – we just launched our new campaign a few weeks ago, "The Sport of Fitness Has Arrived", and we will drive this further and we see very good sell-through across the world, especially on our new products, such as RealFlex which is selling well in Europe. Zig is still doing very well in the US, Japan, Korea. So, the concepts are definitely working.

Obviously, at the moment, we are up against the strong comparables with EasyTone from last year, but the overall business is definitely going in the right direction and you will see this especially in 2013 spring, when we are coming to market with new product concepts and exciting merchandise.

**Robin Stalker**

Jurgen, the simple answer regarding input prices, and given that we don't have a crystal ball for the future years, is that definitely for this year we think the increases have peaked in the first quarter. Therefore we are guiding, obviously, for it to be around what it was at the end of last year for the full year 2012, as this peak is now behind us.

**Jurgen Kolb**

**Okay. And a quick question on hedging. Where are we standing in terms of hedging to the dollar right now?**

**Robin Stalker**

So, for 2012, obviously we are fully hedged at around a 1.37 rate. We're approximately 50% or so hedged for next year and that's at a little bit worse rate, obviously, probably around about 1.35.

**Jurgen Kolb**

**1.35. Very good. Thank you, gentlemen.**

**Michael Kuhn – Deutsche Bank**

**Yes, good afternoon, gentlemen. Firstly, your royalty income was up quite significantly year over year. I think the quarterly report mentions adidas was the major driver behind it. I would be interested in what products drove that development and what we should expect over the upcoming quarters?**

**Secondly, on your opening plans in your store network there are quite some fluctuations right now. Could you give us an indication about what we could expect for the different store categories by the end of the year and also for e-commerce sales? And maybe an indication on what your e-commerce sales were in the first quarter?**

**Finally, I would be interested in a clean Reebok growth figure. Obviously, you gave us a figure ex-toning and ex the license business, but maybe just the underlying development, because I think it's fair to include toning here because that essentially will give the underlying development. Thank you.**

**Robin Stalker**

Michael, yes, you are correct, the royalty income increase is largely because of revenues from the adidas side. Part of this is, particularly this year, related to the products for the events where we have licenses, obviously.

In terms of e-commerce, sales have grown considerably this quarter, up over 60%. And you also had a question about the underlying Reebok growth. Herbert mentioned we had nearly 10% sales growth after we exclude toning, however if we only account for the shift of the NHL and the NFL, then we have a decrease of 5%.

**Michael Kuhn**

**And any indication of the current size of e-commerce?**

**Herbert Hainer**

No Michael, we don't publish any figures for the e-commerce business.

**Michael Kuhn**

**Okay. And then, one follow-up question. I think the question was asked already, and this is nothing on the investigation in India, but could you shed some light on what sales you actually have at your Indian operations to give us a context for the potential one-off costs?**

**Herbert Hainer**

Michael, as we have said, you will understand that we don't comment on the India case, because it is an on going investigation. In terms of size, we do not publish any numbers for individual countries. However, I can tell you that India is not one of our three biggest countries in Asia, which are China, Japan and Korea.

**Michael Kuhn**

**One last question regarding your guidance - you've given a one-off number to us and an operating margin approaching 8%. If we strip out the one-off effect, we are probably at around 8.5% or approaching 8.5%. Is that a fair assumption to use this as a clean number? And could we, thereby, derive an operating leverage for this year of about 90 bps?**

**Robin Stalker**

Michael, I understand the calculation which you would love to have us confirm, but we're not going to do that at the moment. I think you're identifying a couple of areas. We are seeing that we are delivering leverage and obviously this year we have some one-offs. Exactly how high those one-offs are we'll be able to quantify better for you as we go through this year and I'm sure they'll confirm a good underlying improvement in our profitability. But we cannot give you anything other than what we've just given to you in our guidance already today.

**Michael Kuhn**

**Okay. Thank you very much.**

**Antoine Belge – HSBC**

**First of all, can you come back a bit on the performance in Greater China, which was very strong? How confident can we be that this growth has been also reflected in a strong sell-out and not just feeding through the distribution in China?**

**My second question is on SG&A. I think you mentioned that, quite rightly, over the last couple of quarters you have been showing some leverage. What about Q2 and Q3 on the back of the events?**

**Shouldn't we expect that there could be some negative leverage with a lot of spending on the back of the events?**

**And finally, regarding the margin of the Group in the US, and I know that you don't disclose margins by such specific geographies, but in your guidance for 2012 where margins overall are increasing, what would be the contribution of margin in the US? Do you expect those to increase or, because of Reebok, could it be a bit more flattish in terms of margin in the US, for this year? Thank you.**

**Herbert Hainer**

So let me start with the first one, China. Obviously, you have seen China as the star in the first quarter, but also when you look back in 2011, where we have been growing already by around 20%. And remember, two years ago we told you that we will patiently build our China business back after the financial crisis with a much more sustainable and healthy business model. And this is what we have done, especially with our key accounts where we are connected via our IT systems such that we can read faster and better what is happening in the stores in China. Therefore, our sell-through numbers are better and our inventory is cleaner. We can monitor it more closely and this 26% increase was not just a one-off. We will continue to see good growth going forward in China. Our inventories are very healthy – being low and with a very good ageing profile. Furthermore, I must say that I've never been more pleased with the China business than I am at the moment and I also foresee for the next years that we can grow our business at a double-digit rate in China.

Your third question was on the margin of the US – we also mentioned that we believe that by raising our profile and, therefore, raising our average selling prices with better and more innovative products we'd strive for better margin. And I think the adizero Crazy Light basketball shoe is the best example. It's the lightest shoe in the basketball industry, has high consumer demand and, therefore, we can raise prices and we can get better margins and we will continue to do so.

**Robin Stalker**

And, Antoine, in terms of the SG&A, there's always going to be fluctuations from quarter to quarter, depending on timing of marketing, and that's going to be the case this year, too. But looking to the full-year guidance, we are gaining more leverage from our operating expenses and this you will see throughout this year. Actually by the end of this year, you will be able to reflect upon that being a contributor to an improvement in our operating margin.

**Antoine Belge**

**Okay, thank you very much. Maybe just to follow up on inventories as a whole – they had a very decent evolution in Q1. Was it something that was only one-off? And what should we expect in terms of inventory growth, especially compared to your top-line growth guidance?**

**Robin Stalker**

This is the standard we have to try to keep, which I was trying to refer to in my prepared comments, obviously we want to be able to be in a position to quickly service the consumers that need and want our products, but at the same time manage our working capital as efficiently as possible. And I think we've shown that the whole Group has a focus on this and that we are continuing to improve this. You've seen it come down as a percentage of growth over the last several quarters. Moreover, the quality of the inventories should be as clean as possible and I think you can see us always striving to have further improvements in that and there were definitely no one-offs in the first quarter that led to this good figure.

**Antoine Belge**

Okay, thank you.

**Emily Tam – Morgan Stanley**

**Good afternoon. Three questions from me. Firstly, can you please give us an update on how the retail rollout of NEO is going? And also, if have you anything further planned for this year and if you have any further comments to add on the performance of the existing Germany stores?**

**Secondly, with regard to China, it's clear that you're taking market share from the local peers. In terms of the sell-out trends in China at your wholesalers, would you be able to give us some colour in terms of how you're doing versus your local and also the international competitors? And do you think that growth can continue to come from floor-space expansion, especially in the higher tier cities?**

**And lastly, on Reebok, do you think that Reebok can continue to sustain its market share in the US this year and also going forward? Thank you.**

**Herbert Hainer**

Let me start with your NEO question. As I said in my speech already, we have opened 8 out of the 10 planned stores in Germany and the two others will follow in the coming weeks. So, all the early indications which we are seeing so far are quite exciting. Nonetheless, I think it's a little bit too early to already draw any conclusions out of it. But we are very happy with store traffic, with how the format is attracting, particularly, the targeted young female consumers, who are coming into our stores. And we are getting extremely good comments when we do our market research regarding the freshness, the colourfulness and the young feeling of the brand. This is all indicating that the assumptions which we took when we entered into the NEO business are the right ones. But, as I also said, we will definitely use 2012 to test new store and retail formats and concepts in Europe. For example the magic mirror, which you might have seen, or new product concepts that we have prepared to roll out in Europe. By the way, as you know, we have approximately 1,000 NEO stores in China and these are also going in the right direction.

On your second question, which brings me immediately to China; honestly, I believe we are not only gaining market share compared to the local competitors, I think we are also gaining when compared to the other international competitors, because I don't think that the market is growing by 26%. And also given that some of the small international brands are currently having a hard time. I can just repeat what I said before. I think we have done our homework in China. We installed a completely new team two and a half years ago and they're working according to our plan and you can see this is definitely paying off.

And last, but not least, Reebok in the US. I think, and this will be confirmed when you talk to retailers, that in the last 24 months we have done a very good job in the US, exciting consumers with new concepts from Reebok, bringing new consumers back to Reebok with EasyTone, with Zig and with Flex. Flex, by the way, is selling extremely well and also Zig is doing well in the US. We are starting to rebuild Classics and as you know we have Swiss Beatz under contract with Reebok and he is helping us with Classics, especially in the celebrity music scene. So all of this is going in the right direction and as I have said, yes with EasyTone we have strong comparisons for the first six months of this year, but, in general, I definitely believe the business is going in the right direction.

**Andrew Mobbs – Redburn Partners**

**Thank you. Two quick questions. The first, I appreciate it varies a lot by brands and market, but could you give us some kind of indication of the average selling price versus volume increase within the Q1 sales growth of 14%?**

**And my second question, you haven't made any comment on the Reebok joint venture situation in Latin America, which impacted, I guess, sales in Q4. Could you give us some indication of what's going on there and is that part of the reason behind the improvement in Q1 versus Q4? Thank you.**

**Robin Stalker**

Andrew, we don't have any colour for you on the average selling prices. We know they're improving, obviously, but I can't break that down for you.

**Herbert Hainer**

And on the Reebok joint venture in Latin America, obviously we don't break it out separately, but you have seen that our business in Latin America in the first quarter on Reebok is good. It's growing. So, we are working closely with our joint venture partner and things are going according to plan. Nevertheless, I think it's also fair to say that we have some hurdles, such as tariffs and import duties, et cetera, in Brazil and Argentina, which doesn't make our life any easier in that market.

**Andrew Mobbs**

**Okay, perfect. A very quick follow-up question – in terms of the inventory growth, could you give some indication of the volume versus price increase within that?**

**Herbert Hainer**

Obviously, because of the input price increases, this immediately brings our inventory value up. But I can't give you the exact number for what it would be in quantity. However, the quantity growth is definitely much lower than the 13% growth in value. This also indicates quite clearly our good inventory management, when you see that on the one hand we are growing 13% and we are bringing our inventory growth down quarter by quarter and also have a very, very young and very healthy inventory, I think that our guys are definitely doing a very good job in managing our inventories.

**Cedric Lecasble – Raymond James Euro Equities**

**I have two follow-up questions. The first one is on the marketing budget. You used to say that an average level for the Group was between 13% and 13.5%. This year is an important year with big events and you are guiding on less than 13% at 12.7%. Does it mean that you are leveraging your marketing expenditure and is this something structural? Do you believe this ratio will continue to be lower than 13% and probably lower than it was in the past, despite big events?**

**And question number two is on Reebok, we understand the phasing between toning with still strong comps. Easier comps going forward, still declining total sales and to ramp up into the other products, when do you think the balance of the two will lead to more positive growth trends for Reebok, overall? Thank you.**

**Herbert Hainer**

So, on your first question on marketing budget – I think we always have said that we will spend between 12% and 13% and you should not assume that in an event year our marketing working budget is going across this boundary. As we have said already several times, we are phasing our

product introductions, our new brand campaigns and also the big sporting events throughout the years so that we have more or less stable spending on our marketing working budget. Therefore, we are permanently talking to our consumers during the event years and also during the non-event years, with the non-event years being much more focused on product concepts and new innovations, whereas in the event years we are more focused on the events.

And, as you can imagine, with the sales growth which we are experiencing, we want to bring the marketing working budget slightly down, on a step-by-step basis. Nevertheless, let me also make it clear that I see marketing working budget as an investment in our consumers and therefore, we will always spend a certain amount, which we think we need to excite our consumers and drive our sales.

On your second question, on Reebok – I think you can expect a better like-for-like comparison in the second half of 2012, as the toning influence from the strong first half of 2011 will have less of an effect.

**Cedric Lecasble**

**Could you address, maybe, the share of toning sales in the total sales, just to have an idea of when this toning effect is over?**

**Herbert Hainer**

No, we don't comment on any shares of product concepts within total sales.

**Cedric Lecasble**

**Okay. So, you are expecting better growth or positive growth for Reebok in the second half of 2012?**

**Herbert Hainer**

No, and let me be clear on this, we don't see toning as completely over. We believe that we can rebuild the toning business. Obviously, as you know, one of our competitors has put a lot of inventory into the market with low sales and this hurt the market in 2011 and this is continuing into 2012. But we definitely believe in the toning business. All the market research that we are doing is clearly telling us that a) that there is a consumer out there who is excited by the product and b) that Reebok has definitely been the brand which has been the most innovative on the toning side. And this is what we want to use and we still have a lot of countries where toning is doing very well, especially in Asia, but also in Russia, in some of the emerging markets. Therefore, we will come back with the first new collection in the second half of 2012 and then, in spring/summer 2013, you will see a complete new array of toning products.

**John Paul O'Meara**

Ladies and gentlemen, that completes our call for today. We'll report our first half-year results on the 2nd of August, and as Herbert teased in his comments, we will also be hosting an investor trip this year to the United States in September and we will provide more details on that over the next few days.

So, thank you very much and enjoy the rest of your day.