

SOCIAL AND ENVIRONMENTAL REPORT 2002



BEHIND OUR BRAND

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SOCIAL AND ENVIRONMENTAL
REPORT 2002

BEHIND OUR BRAND

2002 WAS A YEAR THAT MARKED A SIGNIFICANT CHANGE IN THE WAY WE WORK WITH OUR SUPPLIERS. THIS REPORT EXPLAINS HOW WE ARE BEGINNING TO CREATE DEEPER BUSINESS PARTNERSHIPS WITH THEM, AND WHY WE BELIEVE THIS STRATEGY WILL LEAD TO IMPROVED LABOUR AND ENVIRONMENTAL STANDARDS THROUGHOUT OUR SUPPLY CHAIN.

THE NEXT FEW PAGES PROVIDE AN INTRODUCTION TO SOME OF THE MAIN SUSTAINABILITY ISSUES WE FACE. TOGETHER WITH OUR MAIN REPORT, BEGINNING ON PAGE 12, IT SHOWS HOW WE ATTEMPT TO GO BEHIND THE PUBLIC FACE OF SPORT IN ORDER TO ADDRESS OUR GLOBAL RESPONSIBILITIES.

AN INTRODUCTION TO THE ISSUES WE FACE

ANY COMPANY THAT WANTS TO MANAGE ITS IMPACTS ON PEOPLE, SOCIETY AND THE ENVIRONMENT NEEDS TO START BY UNDERSTANDING THE NATURE OF ITS BUSINESS. WE UNDERSTAND THAT SOME OF THE BIGGEST ISSUES WE FACE, AND THE ONES THAT PEOPLE ARE MOST CONCERNED ABOUT, ARE ISSUES RELATED TO WORKING CONDITIONS IN THE FACTORIES THAT MAKE OUR PRODUCTS.

Find out how we are monitoring labour standards in our factories
Fair wages 33 /// Child labour 34 /// Labour rights 35 ///

A person wearing a blue long-sleeved shirt, a black helmet, and black goggles. They have their arms raised in a fist, suggesting a protest or a moment of triumph. The background is a solid light blue color. A white rounded rectangle is overlaid on the person's chest.

LABOUR RIGHTS



**HEALTH
AND SAFETY**

BECAUSE WE DON'T HAVE DIRECT CONTROL OVER THESE FACTORIES, IT'S HARDER TO MAKE SURE THAT THEIR CONDITIONS AND EMPLOYMENT STANDARDS ARE DECENT. THAT DOESN'T MEAN WE DON'T TAKE RESPONSIBILITY FOR HOW FACTORY WORKERS ARE TREATED. OUR GOAL IS TO FIND THE MOST ACCEPTABLE SOURCES OF SUPPLY THAT MEET ALL OUR CRITERIA, NOT SIMPLY THE CHEAPEST.

WE JUDGE LABOUR STANDARDS THROUGH OUR CODE OF CONDUCT, WHICH WE CALL OUR 'STANDARDS OF ENGAGEMENT'. THESE ARE GUIDING PRINCIPLES COVERING ALL SORTS OF EMPLOYMENT ISSUES, INCLUDING WORKERS' RIGHTS, THE ENVIRONMENT, AND HEALTH AND SAFETY. BASED ON INTERNATIONAL LAWS, CONVENTIONS AND PRINCIPLES, THE STANDARDS HELP US TO CHOOSE THE FACTORIES WE WANT TO WORK WITH.

Learn how we are attempting to reduce our environmental impacts
Hazardous substances 41 /// Transportation 43 /// Progress against targets 46 ///



THE ENVIRONMENT



**COMMUNITY
INVOLVEMENT**

AS WELL AS HELPING US SPOT PROBLEMS, WE USE THE STANDARDS OF ENGAGEMENT TO HELP FACTORY MANAGERS PLAN HOW TO IMPROVE THE WAY THEIR FACTORIES ARE RUN. TOGETHER WITH INDEPENDENT AUDITORS, WE CHECK PROGRESS REGULARLY. ALL OF THE FACTORIES WE WORK WITH MUST BE ABLE TO SHOW THEY ARE MAKING CONTINUAL IMPROVEMENTS IN ORDER TO MEASURE UP TO THE STANDARDS.

STANDARDS OF ENGAGEMENT

Authenticity / Inspiration / Commitment / 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 consistent 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.

SOCIAL AND ENVIRONMENTAL REPORT 2002

THREE YEARS ON FROM OUR FIRST SOCIAL AND ENVIRONMENTAL REPORT, WE REMAIN COMMITTED TO REGULAR, TRANSPARENT COMMUNICATION OF OUR SUSTAINABILITY PERFORMANCE. THIS REPORT RECORDS OUR EFFORTS TO IMPROVE THE WAY IN WHICH WE ENGAGE WITH STAKEHOLDERS AND TO CREATE MORE PRODUCTIVE PARTNERSHIPS WITH OUR SUPPLY CHAIN. IT ALSO SETS OUT STRATEGIES AND TARGETS FOR NEXT YEAR.

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CEO statement /// CORPORATE RESPONSIBILITY CONTINUES TO BE AN IMPORTANT TOPIC IN THE THREE YEARS SINCE adidas-Salomon PUBLISHED ITS FIRST SOCIAL AND ENVIRONMENTAL REPORT. RECENT GLOBAL EVENTS HAVE GIVEN AN EVEN GREATER URGENCY TO ISSUES THAT ARE CENTRAL TO SUSTAINABILITY, SUCH AS RESPONSIBILITY, HONESTY AND TRANSPARENCY. IN THIS, OUR THIRD REPORT, WE REVIEW OUR ACHIEVEMENTS AGAINST THE 2002 TARGETS AND COMMIT TO OUR 2003 GOALS.

Trust has become a valuable commodity; something that can be achieved only through honesty, open dialogue and a genuine commitment to sustainable development. More than ever before, people are beginning to realise that brands are only as strong as the values that lie behind them. This is something that adidas-Salomon firmly believes in, and has demonstrated throughout this report.

Our Group's mission is to be the global leader in the sporting goods industry. Achieving this goal requires more than outstanding financial performance. It means regarding our economic, social and environmental performance as equally important, integrated elements in a long-term process of continual improvement. As the expectations of our stakeholders continue to increase, so we must constantly be prepared to set new and more demanding performance standards. If this sounds challenging, consider what we have accomplished in 2002 – a year in which adidas-Salomon once again demonstrated its vision and leadership in the field of corporate citizenship.

Nowhere was this more apparent than in our new strategy for our future relationship with our supply chain. While we will continue to validate and monitor supply chain performance, we believe the most effective route to sustainability lies not just in policing our suppliers, but in working in partnership to help them achieve the capacity to take charge of their own sustainability initiatives, based on our Standards of Engagement. We are already beginning to see this drive towards self-governance translated into improved social and environmental performance within our supply chain.

2002 was also a year in which we made progress in engaging with our stakeholders on a diverse range of issues and concerns. For the first time, we introduced a series of structured stakeholder meetings, and responded to every stakeholder enquiry we received. This dialogue proved invaluable in helping us understand and respond to the concerns of those who have a vested interest in our Group. Their feedback is also one of the reasons why this report focuses largely on supply chain performance.

This year's report moves a step closer to the guidelines set out by the Global Reporting Initiative and the last pages of this report provide a gap analysis of where we are already delivering on the guidelines, and where work remains to be done to conform to internationally recognised benchmarks. Our commitment and achievements have been rewarded in the last year: adidas-Salomon continues to be ranked as one of the top companies in its class by the Dow Jones Sustainability Index, the world's leading index for sustainable companies, as well as being included in the FTSE4Good Europe index.

While we can be proud of our achievements over the last year, we remain aware of the challenges that lie ahead. We recognise that significant improvements can still be made in the way we rate the performance of our factories. Although we had hoped to replace our five-star factory rating system with a more rigorous audit method, we have found it difficult to develop the standard measures that would allow us to achieve this effectively. However, we are currently in consultation with a range of stakeholder groups, including factory staff and NGOs, who are helping us develop the standards, and we are confident that we will be able to launch the new factory rating system in 2003.

To return to my initial theme, trust has to be earned. The only way to earn trust is to deliver on the targets you set for yourself. On page 48 of this report, we have set out a list of social and environmental targets we want to achieve in 2003. This is our commitment to continue to improve our sustainability performance. By continuing to work in partnership with all of our stakeholders, we believe we can achieve substantial progress in 2003.



Herbert Hainer
CEO and Chairman of the Board

OUR BUSINESS

Vision and strategy /// WE BELIEVE THAT ACTING AS GOOD CORPORATE CITIZENS LEADS US TOWARDS BECOMING A SUSTAINABLE COMPANY. WE HAVE OUTSOURCED OUR SUPPLY CHAIN, BUT WE HAVE NOT OUTSOURCED MORAL RESPONSIBILITY FOR THE WAY OUR PRODUCTS ARE MADE. OUR VISION IS THAT ALL PARTS OF THE BUSINESS – INCLUDING OUR SUPPLIERS – SHARE A COMMON SET OF VALUES AND UNDERSTAND HOW TO LIVE UP TO THEM.

adidas-Salomon strives to be the global leader in the sporting goods industry with sports brands built on a passion for competition and a sporting lifestyle. This means adidas-Salomon:

- is consumer focused. We continuously improve the quality, look, feel and image of our products to match and exceed consumer expectations
- strives to bring technical and design innovation to footwear, apparel and hardware products, to help athletes of all skill levels achieve peak performance
- is a global organisation that is socially and environmentally responsible, creative and financially rewarding for employees and shareholders.

Our long-term strategy is to strengthen our brands and products continuously, to improve our competitive position and financial performance. It is based on the Group's values – authenticity, inspiration, honesty, commitment – which derive from sport.

RESPONDING TO BUSINESS CHALLENGES While our strategy is simple and our commitment to it is constant, the world in which we operate is complex and highly dynamic. Fast-moving consumer trends, the need for quick market response, permanent product- and process-related innovations and a global supply network determine the business environment and require the Group to plan its future systematically.

This dynamic environment increases pressure on employees, suppliers, the environment and the communities in which we work. It also allows for innovation in planning and execution.

With the help of our stakeholders, we have identified some of the key sustainability issues we face:

- keeping prices competitive without compromising social and environmental standards
- maintaining sustainability while introducing innovative component materials and complex fabrication processes
- meeting unforeseen consumer demand while keeping working hours within the maximum 60-hour week
- enforcing compliance with our standards in countries where there may be no local regulations governing manufacturing
- building and maintaining Standards of Engagement (SOE) compliance within supply chains that are mobile and migratory
- finding a sustainable formula for a fair wage within unskilled, low-tech industries
- improving production efficiency without adversely affecting factory wages and employment levels
- meeting tighter delivery deadlines without cutting corners on compliance
- balancing the risks and the advantages of transparent reporting.

These complex issues would be difficult to address on our own. That is why we are committed to a process of collaboration and open discussion with stakeholders. Stakeholder dialogue has helped us to understand that working conditions in our suppliers' factories is the most important issue for us to tackle. To that end we have established a process of monitoring, validation and training.

From compliance to self-governance Before suppliers can become approved business partners, they must be able to show that their standards and conditions comply with our SOE. However, we regard compliance as just the first stage of a longer term process. We want our suppliers to move on from simply adopting the standards, through to integrating them fully into their general management and decision-making, and finally towards a system of self-governance. Instead of acting as police, we want to work in partnership with our suppliers, helping them to develop and monitor their own sustainability initiatives using our SOE as a baseline.

We cannot achieve this through monitoring alone. While we continue to monitor and audit problem factories, we are increasingly involved in running or facilitating training programmes with the factories, managers and workers, in order to give them the skills and knowledge to create and take leadership of their own policies and initiatives.

The case for sustainability We believe that managing our supply chain responsibly and reducing our environmental impacts will improve our corporate reputation and hence our economic value. We also believe that treating people with dignity and respect is a basic right that should be extended to all. To ensure this, we have created a set of sustainability principles that guide our work in this area. These principles, which include our commitment to reporting our social and environmental performance regularly and transparently, underpin the approach we take in the initiatives described throughout this report.

SUSTAINABILITY PRINCIPLES ///

LEGISLATION We adhere to social and environmental laws, directives and guidelines while continually improving 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 clear targets; formulate action plans, monitor progress and publish the results.

SUPPLIER AND CUSTOMER RELATIONSHIPS We expect suppliers' activities to be compatible with the adidas-Salomon Standards of Engagement. We encourage our business partners to take a proactive stance on the social and environmental impact of their activities, and work in partnership to improve our collective performance.

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 regularly provide appropriate information about the Group's social and environmental performance, to encourage an atmosphere of trust and respect.

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. adidas-Salomon SERVES THE WHOLESALE AND RETAIL MARKETS AROUND THE WORLD, BUT ALSO SPONSORS SPORTS CLUBS, 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 the 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, 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 strategic business units for Running, Soccer and Tennis as well as our Research and Development Centre.

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

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

OUR EMPLOYEES At 31 December 2002, adidas-Salomon employed 14,716 people. This represents an increase of six percent from the previous year. In 2002, the largest number of new employees came from the retail sector and the integration of Arc'Teryx into the Group.

adidas-Salomon employees represent a cross-section of cultures, ages and backgrounds. Women account for 44 percent of our employees. 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 2002 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. The stock exchange registration number in Frankfurt (WKN) is 500340 and the ISIN code is DE0005003404.

SUPPLIERS adidas-Salomon works with independent suppliers from around the world who manufacture its products. 51 percent of all factories are located in Asia, with 22 percent in the Americas and 27 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, which source products from 118 suppliers in 21 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 19 show our financial performance in 2002 and compare this with the previous two years.

Number of adidas products manufactured*

	2002	2001	2000
Footwear (millions of pairs)	99.57	81.60	91.70
Apparel (millions of units)	129.30	125.60	122.90
Hardware** (millions of units)	24.43	17.90	18.90

* International market

** Accessories and gear

Number of Salomon products manufactured

	2002	2001	2000
SNOWBOARD (MILLIONS OF UNITS)			
Board	0.12	0.13	0.13
Binding	0.12	0.12	0.12
ALPINE (MILLIONS OF UNITS)			
Ski	0.74	0.83	0.77
Binding	1.30	1.30	1.20
Boots (pairs)	1.14	1.10	1.00
CROSS-COUNTRY (MILLIONS OF UNITS)			
Binding	0.68	0.80	0.86
Boots (pairs)	0.46	0.38	0.45
TEC HIKING (MILLIONS OF PAIRS)			
Boots	0.07	0.20	0.38
INLINE SKATES (MILLIONS OF PAIRS)			
ILS	0.31	0.62	0.78
MAVIC (MILLIONS OF PAIRS)			
Rims	1.70	1.63	2.05
Wheels	0.45	0.39	0.27

Number of TaylorMade-adidas Golf products manufactured

	2002	2001	2000
HARDWARE (MILLIONS OF UNITS)			
Woods	1.45	1.11	0.95
Irons	1.66	2.06	1.66
Putters	0.18	0.14	0.13
Kids Clubs	0.01	0.01	-
SOFT GOODS (MILLIONS OF UNITS)*			
Bags	0.17	0.06	0.21
Gloves	0.28	0.13	0.52
Balls**	4.49***	0.51	1.26
Caps	0.32	0.17	0.40
Accessories	0.38	0.18	0.27

* Excluding adidas Golf

** Reflected as dozens

*** Balls for 2002 produced by Dunlop Slazenger

Net sales by brand

Net sales (euros in millions)	2002	2001	2000
adidas	5,105	4,825	4,672
Salomon	684	714	703
TaylorMade-adidas Golf	707	545	441

Net sales by region

Net sales (euros in millions)	2002	2001	2000
Europe	3,200	3,066	2,860
North America	1,960	1,818	1,906
Asia	1,166	1,010	875
Latin America	163	178	171

Net sales by main product divisions

Net sales (euros in millions)	2002	2001	2000
Footwear	2,851	2,650	2,516
Apparel	2,288	2,212	2,175
Hardware	1,385	1,250	1,144

Operating highlights

Operating highlights (euros in millions)	2002	2001	2000
Net sales	6,523	6,112	5,835
Income before tax	390	376	347
Net income	229	208	182

Key ratios (%)

Gross margin	43.2	42.6	43.3
Selling, general and administrative expenses as a percentage of net sales	34.4	33.3	34.5
Effective tax rate	37.9	39.0	40.3
Net income as a percentage of net sales	3.5	3.4	3.1
Equity ratio	25.4	24.3	20.3

Per share of common stock (euros)

Basic earnings per share	5.04	4.60	4.01
Dividend per share	1.00*	0.92	0.92
Share price at year end	82.30	84.30	66.00

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

* Subject to Annual General Meeting approval

Corporate governance /// BECOMING A SUSTAINABLE COMPANY DEMANDS BOARD-LEVEL COMMITMENT, INTEGRATED DECISION-MAKING AND STAKEHOLDER DIALOGUE. TO ACHIEVE THIS WE HAVE ESTABLISHED A GOVERNANCE FRAMEWORK THAT IDENTIFIES BOARD-LEVEL RESPONSIBILITY FOR SOCIAL AND ENVIRONMENTAL AFFAIRS AND ALLOWS FOR EACH TO CONTRIBUTE TO AN ANNUAL BUSINESS STRATEGY. THIS IS AGREED BY THE EXECUTIVE BOARD AND AUTHORISED BY THE SUPERVISORY BOARD.

Corporate governance means standards of good and responsible corporate management, which have always been a major priority of our Group. adidas-Salomon welcomes the provisions of the German Corporate Governance Code, which became legally binding for stock-market-listed companies in August 2002. Our Group has prepared its own Corporate Governance Principles which draw on the majority of the recommendations and suggestions of the German Corporate Governance Code. The adidas-Salomon Corporate Governance Principles are designed to achieve responsible corporate management and control with the emphasis on added value, and are intended to promote confidence in our Group on the part of all its stakeholders: current and future shareholders, lenders, employees, business associates and the public. Our Supervisory Board, Executive Board and senior managers identify with these principles and are committed to them.

The adidas-Salomon Corporate Governance Principles contain provisions governing the responsibilities and duties of the Executive Board and the Supervisory Board, collaboration between the Executive Board and Supervisory Board, information and disclosure obligations and the resolution of any conflicts of interest.

Shareholders in adidas-Salomon AG exercise voting rights at Annual General Meetings. They receive regular information in the form of a financial calendar, the annual report, quarterly reports and reports covering social and environmental issues.

The Executive Board currently consists of seven members. It formulates the strategy and direction of the Group, agrees this with the Supervisory Board and ensures that it is put into practice. It ensures that the appropriate risk-management and risk-monitoring procedures are in place and guarantees

the observance and continued development of the company's own SOE, which set out the Group's position with regard to the social and environmental issues facing society.

The Supervisory Board consists of 12 members, six of them elected by the Annual General Meeting and six by employees in accordance with the provisions of the German Law on Co-Determination. It regularly advises and supervises the Executive Board in its management of the company, constantly receiving comprehensive, up-to-date information from the Executive Board in respect of all matters relevant to corporate planning and strategic development, the progress of transactions and risk management. It is also responsible for the appointment and dismissal of Executive Board members.

As an example of good corporate management, the Group has set up a European works council. This is currently made up of 13 delegated employee representatives from European subsidiaries of the adidas-Salomon Group. Its work revolves around social dialogue with the Executive Board of adidas-Salomon AG, in the form of consultations and the exchange of information at regular meetings.

Summary

- adidas-Salomon complies with the overwhelming majority of the recommendations of the German Corporate Governance Code. In December 2002 it published a declaration of compliance, listing discrepancies.
- In early 2003, our Group published the adidas-Salomon Corporate Governance Principles.

For more information about corporate governance please visit our corporate website at www.adidas-Salomon.com

Governance structure

SUPERVISORY BOARD

Henri Filho, Chairman
 Dr. Hans Friderichs, Deputy Chairman
 Fritz Kammerer, Deputy Chairman
 Sabine Bauer
 Gerold Brandt
 David Bromilow

Herbert Müller
 Hans Rupprecht
 Charles Thomas Scott
 Heidi Thaler-Veh
 Christian Tourres
 Klaus Weiß

EXECUTIVE BOARD

Herbert Hainer, CEO
 Glenn Bennett, Global Operations
 Manfred Ihle, Legal and
 Environmental Affairs
 Ross McMullin, North America

Michel Perraudin, Global Human
 Resources, Key Projects and
 Corporate Services
 Robin J. Stalker, Finance
 Erich Stamminger, Global Marketing

FROM GOVERNANCE TO ACTION Every year the Executive Board prepares a strategic business plan, for which the approval of the Supervisory Board must be obtained. The strategic business plan not only anticipates business opportunities and threats, but also standardises goals and targets across various corporate functions and divisions.

Social and Environmental Affairs (SEA) is one such function. Its Global Director reports directly to Manfred Ihle, General Counsel and Member of the Executive Board, responsible for Legal and Environmental Affairs.

The members of the SEA team include engineers, lawyers, HR managers, former members of non-governmental organisations (NGOs) and experienced industrial managers. The team is organised in three regional teams covering Asia, America and Europe (including Africa). It collaborates closely with the global operations group, which is responsible for sourcing products from suppliers. SEA also works with other departments in the company, including those involved in marketing, development, sales and human resources. An example of this is the SEA team's involvement in the development of a corporate policy on charitable donations. This is nearing completion, and a report will be issued in 2003.

The SEA team has developed its own rolling three-year strategy covering the activities of its 30 staff in Asia, Europe and the Americas. The strategy focuses on certain key areas in which the team acts or has influence. The key areas are:

Management Development of management practices to support the integration of the principles of sustainability within all functional divisions of the adidas-Salomon Group.

Suppliers Capacity-building within the workforce and the management of our supply chain to ensure fair and safe working conditions. We will continue to develop 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.

Continuous improvement in labour and health and safety Addressing employment issues and conditions within the workplace in a timely and relevant manner.

Environment Raising environmental awareness internally and externally, and promoting environmental best practice. We will promote the creation and implementation of products and services that do not have a negative impact on the environment.

Community Engaging with stakeholders in the communities where our products are made, we will continue to develop our programmes of corporate donation and local community involvement, both at the supplier level and where our own facilities are located.

Each year the SEA team prepares an operational plan containing details of how the strategy will be implemented. This year the focus has been on improving internal processes, changing the way we work with suppliers and extending our stakeholder dialogue programme.

SOE PROGRAMME The SEA team uses the SOE as a tool to select potential suppliers and to monitor and validate their performance. The SOE are the principles that guide our work with the supply chain, helping to bring about improvements and to report the results with maximum transparency.

Stakeholders /// BY ACTIVELY AND SYSTEMATICALLY ENGAGING WITH STAKEHOLDERS, AND INVOLVING THEM IN THE KEY DECISIONS THAT SHAPE DAY-TO-DAY OPERATIONS, WE BELIEVE WE CAN BALANCE INTERESTS, BUILD CONSENSUS AND ENHANCE THE TRANSPARENCY OF OUR BUSINESS. WE PURSUE A POLICY OF OPEN DIALOGUE WITH STAKEHOLDERS – DEBATING ISSUES AND APPROACHES AND, WHERE APPROPRIATE, FORMING PARTNERSHIPS TO DEVELOP LONG-TERM SOLUTIONS.

IDENTIFYING STAKEHOLDER GROUPS The 2001 report defined stakeholders as those whom we affect and who affect us. This is a very diverse range of organisations, groups and people, and includes concerned consumers, employees, workers in our suppliers' factories and NGOs.

Not all of our stakeholders have a voice. We are still looking for ways to improve how we communicate with, and receive feedback from, all of our stakeholders. Our global social and environmental reporting initiative, launched in early 2001, was the first step in this process. This year, we have also begun to hold formal consultation meetings – we call them 'stakeholder dialogues' – to engage key stakeholders and canvas their views on our SOE programme. These dialogue meetings supplement the many individual points of contact, meetings and enquiries from stakeholders during the course of the year.

If we are to gauge the effectiveness of our current efforts and choose the right path for future actions, regular stakeholder dialogue and feedback is essential. From 2003 onward, stakeholder meetings will take place annually in each of the three key sourcing regions: Asia, the Americas and Europe.

TYPES OF ENGAGEMENT In addition to the stakeholder dialogue sessions described above, we use a variety of techniques to engage with our stakeholders. The Works Council and one German union is represented on the Supervisory Board of the Group, so there is constant collaboration between management and staff. We conduct surveys with our staff to determine their views on social responsibility. We have convened roundtable discussions with external stakeholders in Asia, Europe and the Americas. We also work with other companies through memberships in trade associations and collaborative programmes to improve the way we work with suppliers and communicate with stakeholders.

Staff and management surveys In the first half of 2002 we conducted two internal surveys: one of staff, the other a cross-section of senior management. The primary purpose of the surveys was to gauge internal understanding of and support for the SOE programme and to measure the effectiveness of internal communication and training on social and environmental issues.

The results show that employees feel it is important to work for a company that tackles social issues and that they believe adidas-Salomon to be an environmentally and socially responsible company. Employees also strongly supported the need to report on social and environmental issues internally, as we do externally. Overall, 72 percent of respondents confirmed they had heard of the SOE, with fewer knowing this term in Asia (63 percent) than in the Americas (67 percent) or Europe (94 percent). To close this gap in knowledge and understanding we are planning to make the 2002 social and environmental report available to every employee.

The senior management survey showed strong support for the SOE programme. Of senior managers, 94 percent believe that SOE monitoring activities add value to the Group's performance and that formal reporting mechanisms support internal communications, but increased SOE training should be given. All managers believed that the SOE had brought about a positive improvement in factory conditions, with the same percentage acknowledging that the long-term future of SOE relies on factories developing their own internal systems and capabilities.

Respondents were also asked to rank the purpose of social and environmental compliance, based on six optional statements. The ranking reveals the importance given to SOE in bringing about factory improvement, in promoting the core values of the Group and in safeguarding against risks to the Group's reputation. Interestingly, managers gave the lowest ranking to SOE as a means of competitive advantage, and of safeguarding against media or NGO criticism.

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

STAKEHOLDER FEEDBACK

SUMMARY OF STAKEHOLDER MEETINGS /// Meeting participants were given copies of the 2001 Social and Environmental report and asked to comment on both the report and on adidas-Salomon's social and environmental programme. A summary of participants' feedback follows.

- Participants raised the need to prioritise supply chain policy implementation at both headquarters level and in the workplace in the countries where products are manufactured.
- Participants asked adidas-Salomon to increase its leverage with factory owners to improve overall compliance levels and working conditions.
- The general view was that, in order to change working conditions in developing countries, it is essential that companies influence and build local government capacity to enforce their own labour standards. One said: 'Does adidas recognise its responsibility to tell governments that the company expects and encourages better enforcement of local labour laws?'
- While praising adidas-Salomon's efforts to engage with stakeholders, participants encouraged us to widen the scope of interaction and develop country-specific dialogue. 'You have to divest yourself of some of your power by building a local process.'
- Participants widely

supported the notion of transparency, with opinion varying on the degree of information that should be shared with the public. 'The information about grading factories is tantalising, but where are the elements of your grade? Where is the hard data?'

- Some of the participants believed that labour organisations should have greater representation in stakeholder discussions. 'You'd have greater legitimacy with more workers' voices.'

It was suggested that adidas-Salomon's own Works Council, which represents the interests of the employees, could be invited to future stakeholder meetings.

- It was felt that there should be a continuing effort to develop and refine the internal management systems for administering the SOE, including independent verification structures. 'Is the code applied in the same way in China as it is in El Salvador?'
- Participants emphasised the critical importance of a living wage. 'Until you

implement a living wage policy, you're still running sweatshops and contributing to poverty.'

- Some participants at the London meeting felt that adidas-Salomon's monitoring and verification model should have a greater European orientation, with global convergence of monitoring systems in the longer term.
- Generally, impressions of the 2001 report were quite positive, with participants looking most favourably upon the honest tone of the report, and adidas-Salomon's clear acknowledgement of the need for continual improvement. 'It demonstrably has more in it and more candour than others. It goes a long way towards convincing advocates that adidas is serious.'
- Participants were pleased with adidas-Salomon's attitude throughout this process, and characterised it as a dialogue. 'You do listen. You learn, and you also push back sometimes. It tells something about the openness of management, rather than arrogance.'

RESPONDING TO FEEDBACK /// We would like to thank all those who have given us feedback about our policies, operations and reporting. We took into account the valuable comments provided at the stakeholder meetings when we finalised our Operation Plan for 2003. We proposed:

- disclosing our supplier termination policy in case of SOE-breaches
- increasing transparency in the grading system we will partner a collaborative project with a NGO
- requesting the FLA to extend its verification of supplier factories beyond those required in its protocol for a participating company. This includes those football factories not covered by the International Labour Organization (ILO)

- splitting the planned stakeholder dialogue in Asia into two meetings, one to be hosted in Southern China and the other possibly in Vietnam, in order to increase local, in-country dialogue
- moving our social and environmental reporting closer to the guidelines of the Global Reporting Initiative
- discussing the outcome of the living wage study with a broader audience in 2003
- creating different makeup of participation in future

European and USA stakeholder dialogues. For example, we plan to invite a representative of the adidas-Salomon Works Council to the next stakeholder meeting in Europe

- improving our measuring of the environmental impact of footwear production
- exploring the possibility of having the 2003 report verified independently.

STAKEHOLDER MEETINGS The first formal stakeholder meeting with NGOs took place in Hong Kong in December 2001. Since then we have built on this by coordinating two additional stakeholder meetings in Europe and in North America in 2002. Participants included representatives from other major brands, a trade association, a trade union, a social investment and tracking fund, a sustainability institute, a certification organisation, and a number of human and labour rights NGOs.

Each meeting was managed and recorded by an independent advisor. Business for Social Responsibility (BSR) helped us with the selection of stakeholders in the US and ran the Washington DC meeting. Adrian Henriques, a corporate social responsibility (CSR) consultant, oversaw the European stakeholder meeting in London, England.

RESPONDING TO SPECIFIC FEEDBACK The SEA team engages continuously with local organisations such as NGOs, religious groups, trade unions and other special interest groups. Over the course of the year we have received many enquiries from the media, NGOs, worker rights groups, campaigners, academics, investment funds, students, shareholders and others about suppliers, the SOE programme and our current practice. Where concerns or issues have been raised these have been fully investigated, assessed and a response given. In some cases, we have gone beyond a simple exchange of views, or information, and have worked collaboratively. Issues raised throughout the year include:

- poor working conditions for football manufacturers in mainland China
- underage stitching of footballs in India and Pakistan
- working conditions in the footwear industry in Indonesia
- factory conditions at an accessories factory, Indonesia

- working conditions in an apparel factory, El Salvador
- the use of kangaroo leather in the manufacture of soccer boots
- apparel factory closure in Thailand.

Details of how we respond to stakeholder feedback can be found at www.adidas-Salomon.com/en/sustainability/archive/

Collaborative efforts following feedback, PT Dada, Indonesia

The Workers Rights Consortium (WRC) is a non-profit organisation that helps to enforce manufacturing Codes of Conduct adopted by US colleges and universities. In 2002, the WRC published two reports covering its investigations of PT Dada, an Indonesian factory supplying caps to adidas-Salomon. Since mid-2001, adidas-Salomon had been aware of problems at PT Dada related to working conditions, workers' freedom of association and associated cases of harassment.

From the outset it was agreed that there was a need for constructive dialogue between the WRC, factory management, and adidas-Salomon. adidas-Salomon led with the development and monitoring of action plans, setting timelines and supporting PT Dada with its remediation efforts. These action plans were shared with other buyers and with the WRC, who engaged three local monitors to get independent feedback from workers.

A Remediation Progress Report, published by the WRC in September 2002, detailed changes to their original recommendations and explained additional areas of remediation agreed with adidas-Salomon and PT Dada. The report acknowledges the very significant changes that have taken place at PT Dada and adidas-Salomon's 'heavy efforts on issue-by-issue remediation work'. Not all of the issues at PT Dada have been resolved and the collaborative efforts of the WRC and adidas-Salomon are continuing.

MEMBERSHIP AND COLLABORATION We are actively involved with the World Business Council for Sustainable Development, Business for Social Responsibility, the World Federation of Sporting Goods Industry, the International Labour Organization and the Fair Labor Association. Typically our involvement means that we:

- adhere to and promote codes of conduct
- support independent monitoring and capacity building
- develop and comment on guidelines and industry best practice
- are transparent.

SHARING KNOWLEDGE WITH OTHER BRANDS adidas-Salomon is committed to sharing its knowledge and experience of social and environmental compliance. During 2002 we shared our current guidance materials and other information from the SOE programme with a number of global brands. We used seven shared Fair Labor Association (FLA) audits as an opportunity to collaborate with Reebok and Nike during remediation of audit findings in the Americas, Asia and Europe.

The SEA team is in regular contact with counterparts in Nike, Reebok, Pentland, Puma and other major brands. They also share information with other CSR practitioners at mutually shared factory sites, and at business forums such as conferences and working groups. Every two to three months SEA team members in Hong Kong participate in a Buyers Compliance Group meeting. This meeting offers an informal forum for compliance officers to meet and exchange views on labour rights, legislative changes and other issues.

- Benefits of stakeholder dialogue ///**
- To bring about an improvement to factory conditions
 - To safeguard the Group against risks to reputation
 - To promote the values of the people (and of sport) who work for the Group and make them feel it is worth working for
 - To reduce our legal liabilities as a Group
 - To minimise criticism from the media and NGOs
 - To remain competitive with other brands

Suppliers /// IN 2002 WE CONTINUED TO CONSOLIDATE OUR SUPPLY CHAIN BY PLACING LARGER ORDERS WITH FEWER FACTORIES. INCREASED EFFICIENCIES IN FOOTWEAR MANUFACTURE, AND A CONTINUED FOCUS ON HIGHER PRODUCT QUALITY AND DELIVERY PERFORMANCE, ARE ALSO LEADING TO FEWER SUPPLY PARTNERSHIPS. THIS RESULTED IN DEEPER, MORE PRODUCTIVE BUSINESS RELATIONSHIPS WITH OUR SUPPLIERS AND IMPROVED COMPLIANCE WITH SOCIAL AND ENVIRONMENTAL STANDARDS.

SUPPLY CHAIN STRUCTURE Our supply chain is both global and complex. Some 51 percent of all the factories in our supply chain are based in Asia. Of the remaining factories, 22 percent are in the Americas, and 27 percent in Europe. If we compare this with the figures presented in the 2001 report we see that we have:

- 124 fewer suppliers overall
- more suppliers in: Argentina 9, Brazil 4, Portugal 19, Vietnam 6
- fewer suppliers in: Bulgaria 10, China 9, Indonesia 5, Japan 13, Korea 7, Malaysia 15, South Africa 8, Turkey 14, UK 5, USA 46.

The supply chain comprises many different types of supplier, which can be categorised as follows.

Main factories Factories of suppliers who have a direct contractual business relationship with adidas-Salomon. We term these 'Tier 1' factories. Tier 1 suppliers may be manufacturing adidas-Salomon products for export, or for local market consumption. Factories producing for a domestic market tend to be much smaller than their export counterparts. Local as well as international apparel factories are often family-owned businesses, with anywhere between five and 500 employees. This is in contrast to our large-scale footwear suppliers, where a single factory may employ upwards of 10,000 workers.

Subcontractors Factories that have been subcontracted by our suppliers and do not have a direct contractual relationship to adidas-Salomon.

Material and other service providers Factories that may or may not have a direct business relationship with adidas-Salomon, but supply goods and services to the main factories. We term these 'Tier 2' factories. As with the main Tier 1 factories, Tier 2 suppliers are very diverse in their size and types of operation, from a local printer with five employees printing adidas T-shirts, to an international fabric mill employing many hundreds of workers.

Licensees We have licensing agreements with independent companies who manage the design, manufacture and distribution of specific product lines. Licensees are also required to adhere to the SOE and to check the factories with which they work for quality and SOE compliance.

Number of suppliers and our own factories in 2002

	Supplier main factories	Own factories	Total
ASIA			
adidas	372	1	420
Salomon*	17	0	
TaylorMade-adidas Golf**	29	1	
AMERICAS			
adidas	169	0	182
Salomon*	3	1	
TaylorMade-adidas Golf**	8	1	
EUROPE			
adidas	201	1	226
Salomon*	19	4	
TaylorMade-adidas Golf**	1	0	
Total	819	9	828

* Includes Bonfire, Mavic and Arc'Teryx

** Includes Maxfli

adidas licensees in 2002

	Total no. of licensees	Total no. of factories producing for licensees	No. of countries where production is placed
Apparel	10	99	17
Hardware*	5	13	3
Watches	1	3	2
Glasses	1	2	2
Cosmetics	1	1	1
	18	118**	

* Accessories and gear

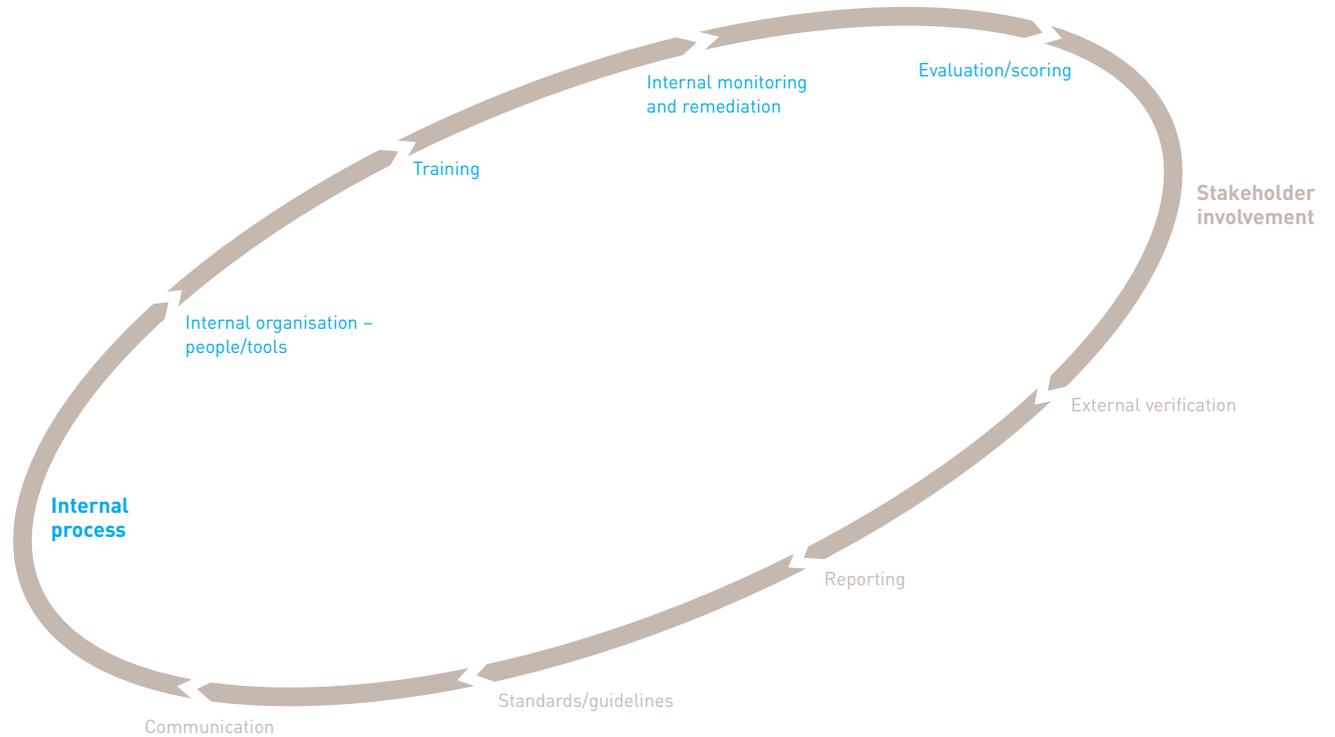
** The 118 factories are placed in 21 different countries

WORKING WITH SUPPLIERS Our strategy is based on a long-term vision of self-governance. Becoming more sustainable requires building up capacities in suppliers' workforces, in their management, in local workers' organisations and NGOs so that acceptable conditions become a routine part of how business is done. To achieve this we aim to continue to move from a monitoring role towards a more support-based role. This means working in partnership with our suppliers and giving them guidance and training where necessary.

The standards and practices we expect our suppliers to follow are set out in our SOE – the Group's code of conduct. (The SOE are shown in full on page 10.) The SOE management cycle helps to ensure compliance with these standards.

SUPPLIERS AND THE SEA TEAM The SEA team is responsible for promoting the SOE among suppliers and checking compliance. They undertake 'pre-approval' audits before a contract is signed with a factory. Suppliers must sign a manufacturing agreement that commits them to complying with the SOE and to communicating these standards to each of their own suppliers. Whenever possible, local field auditors are used, drawing on first-hand knowledge of local regulations and relevant language skills, enabling more effective communication with suppliers and their workers.

The SOE management cycle



Improving SOE compliance ///

The SEA team is currently developing a policy to improve the SOE coverage of the Tier 2 suppliers. These suppliers number in the many thousands, normally have no direct business relationship to adidas-Salomon, and may change frequently, depending on the specific service and material supply requirements of our main suppliers. Some progress has been made in the auditing of material suppliers within footwear for SOE compliance and selective visits have been made to fabric mills in China and Taiwan. Beginning in 2003, all of our Tier 1 business partners will be required to maintain a 'suppliers' register', together with a formal record of their effort to communicate and incorporate the SOE into their dealings with material suppliers, contractors and other service providers.

OUR PERFORMANCE

Improving the way we work with suppliers /// WE HAVE SET IN PLACE PLANS TO DELIVER OUR LONG-TERM VISION OF SUPPLIER SELF-GOVERNANCE, SO THAT MORE OF OUR SUPPLIERS HAVE THE TOOLS TO MAKE ACCEPTABLE WORKPLACE CONDITIONS A ROUTINE PART OF HOW THEY DO BUSINESS. THIS REQUIRES US TO SHIFT THE EMPHASIS OF OUR RELATIONSHIP WITH SUPPLIERS FROM MONITORING TO TRAINING. WHILE WE WILL CONTINUE TO MONITOR FACTORIES AND FOCUS ON THOSE WITH SERIOUS NON-COMPLIANCE ISSUES, WE INTEND TO CARRY OUT MORE FOCUSED TRAINING WITH ALL SUPPLIERS.

Our long-term strategy for self-governance demands that suppliers integrate the SOE into their own systems. To move into the next phase of this strategy, we needed to revise and improve our SOE management cycle.

We have improved internal collaboration between departments that source from supply partners. This has led to a more efficient supply chain and improved social and environmental performance. Particular initiatives conducted during 2002 include:

- improving systems, guidance and training
- developing new policies and management systems
- improving monitoring and verifying systems.

SYSTEMS, GUIDANCE AND TRAINING During 2002, we improved guidance and training to support the SOE programme's work in the field. Auditing tools were revamped to make them easier to use and to measure performance more thoroughly. They were field-tested during the second half of the year.

In addition we published our Guide to Best Environmental Practice and distributed it throughout the supply chain. The Guide clearly explains and promotes sustainability initiatives.

We continued to issue environmental guidelines to all partners and supplementary documents to help our more experienced partners deal with particular issues in more detail.

When we need to alert our partners to major health and safety risks or other significant events, we issue Health, Safety and Environment (HSE) Advisory Notes that describe the issue, what action to take and who to contact for more information.

Since 2000 we have conducted face-to-face training to explain technical issues and share best practice. During 2002, regional SEA teams attended 111 training sessions to build internal capacity and skills. The SEA team then facilitated 255 training sessions with factory workers and management.

POLICIES AND MANAGEMENT SYSTEMS The SEA team encourages suppliers to develop clear policies and procedures to implement SOE within their factories. It is therefore important that SEA team activities and the team's inter-relationship with suppliers is clearly described and understood.

At the beginning of 2002, the SEA team began to develop formal written policies for internal and external communication. In March 2002, we issued an internal policy document to SEA team members describing how to balance the need for increased public transparency with our obligations to suppliers and their workers on confidentiality agreements and privacy issues.

We are developing policies to supplement the technical guidance already in circulation. Early in 2003, a formal policy document will be issued to describe how the SOE should be applied to Tier 2 suppliers (subcontractor and material suppliers). At present our main business partners (Tier 1 suppliers) are asked to communicate the SOE requirements to their respective suppliers. From 2003, our partner factories will be asked to maintain a suppliers' register for review as part of the SEA team's regular monitoring activities.

Suppliers will also be issued with a formal policy document, setting out our approach to enforcement and the possible sanctions that can be imposed due to breaches of the SOE. Sanctions can include the suspension of, or reduction in, orders given to a factory, or in a worst-case situation can lead to the termination of a manufacturing agreement. Termination is seen as the last resort and is only considered where all other remediation efforts have failed to resolve issues.

Warning system At the beginning of 2002, the SEA team introduced a system of warning letters. A first warning is issued when the team finds a factory has serious labour or health and safety (H&S) problems. An action plan is devised to manage the

Training in 2002 divided by region and type

Region	General SOE training	Specific labour training	Specific HSE training	Total
Asia	93	43	7	143
Americas	12	6	4	22
Europe	86	4	0	90
Total global	191	53	11	255

Examples of training

General SOE training: practical on-site training; presentations for awareness raising.

Specific labour training: worker-management communication; sharing best practice; freedom of association; factory overtime system; grievance & appeal systems.

Specific HSE training: sharing best practice; chemicals in production.

Number of business relationship terminations due to SOE problems in 2002

Reasons for termination / SOE problems		Terminations per country
ASIA		
China	Wages and benefits, working hours, serious HSE problems, poor cooperation with SEA team	9
Indonesia	Wages and benefits, working hours, serious HSE problems, poor record keeping, no real keenness to improve SOE conditions	2
Philippines	Excessive working hours, Sunday work, various HSE problems	2
AMERICAS		0
EUROPE		
Estonia	Serious HSE problems and no response to our action plan	1
GLOBAL		14

problem. Failure to implement the action plan often reflects a poor management attitude towards the workforce. In these cases the factory owner is informed that their partnership with adidas-Salomon is in jeopardy. If the action plan is not implemented within the agreed timelines, a second warning is given. If, following that, the breach remains unresolved, a third and final warning follows.

To date, 14 suppliers have received a first warning about an ongoing violation or a lack of progress or commitment to SOE. All of these were located in Asia. There were no second or third warnings issued in 2002.

Lean – opportunities and challenges Lean is our new efficiency initiative designed to improve overall factory performance in terms of delivery, quality and cost. Recently implemented by all of our footwear suppliers and many apparel and hardware suppliers, Lean requires factories to review their operations critically and to improve their production rates by adopting new and more efficient processes and providing workers with special training. In doing so, it offers opportunities for factories to improve workplace health and safety and labour practices, increase communication between workers and management and reduce working hours.

Lean presents challenges as well as benefits from an SOE perspective. As factories experiment with new layouts and working systems, and install new equipment, it is important to make sure that labour and H&S standards are not compromised. The SEA team has therefore developed a simple set of H&S principles to apply when production lines are re-arranged or machinery is repositioned.

With reduced overtime, some Lean apparel factories report increased turnover rates as workers seek jobs with neighbouring factories where long overtime hours are still the norm and employees can maximise earnings. This indicates that payroll structures are out of step with the changes taking place in production. The SEA team is examining factory pay structures and incentive programmes, to see whether there are better ways to reward workers for their increased skills and productivity.

Successful implementation of both Lean and SOE depends largely on sustained improvements in management systems. Lean requires factories to maintain better records, and to document systems and procedures. For example, a specific job function on a production line must be properly identified, examined and then described in writing. Such job descriptions may be used in cross-training materials, posted at the job location itself, and used in performance evaluation and promotion forms. Similarly, the SOE requirements demand good record keeping by administrative, human resources and production staff. This is the fundamental basis of effective and transparent management of people and their work. The SEA team works closely with the management during factory visits and supplier training sessions to develop a culture of transparent documentation of systems and procedures.

MONITORING AND VERIFICATION

External independent monitoring adidas-Salomon was a board member of the FLA in 2002. This independent monitoring organisation completed its first year of monitoring in August 2002. The FLA model is innovative because it is collaborative, bringing together companies, non-governmental organisations, colleges and universities.

FLA participating companies performed more than 2,000 internal supplier audits. There were more than 220 external, independent factory audits conducted by FLA independent monitors, with adidas-Salomon contracted factories participating in 42 of those audits. This fulfilled our obligations to independent external monitoring under FLA charter guidelines. Corrective action plans for the 42 FLA sites were developed and have been incorporated into current internal SOE monitoring plans. In 2003, at least five percent of the supply chain will be monitored by the FLA, which will choose both factories and monitors.

Additional independent monitoring programmes were executed at selected supplier factories by the ILO in Pakistan and Cambodia and by Societe Generale de Surveillance (SGS) in India (see page 34).

Notes to table overleaf: Number of factories audited in 2002

The table on the next two pages 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 how many factories we audited in 2002 to the total number of supplier factories operating in that country, grouping the countries into three regions: Asia, the Americas and Europe*.

In some instances the table shows that we have audited more factories than we now have in a particular country. This is because we have terminated our business relationship with some of the factories, either due to SOE problems or to consolidate our supply chain. For details of the number of factories whose contracts we terminated due to SOE non-compliance, see the table opposite.

* To reflect the way our SOE 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, New Zealand and Mauritius are included under Asia.

Number of factories audited in 2002

Country	Total number of factories	Number of audited factories	APPAREL				HARDWARE*				FOOTWEAR			
			Main factories		Subcontractors		Main factories		Subcontractors		Main factories		Subcontractors	
			Total	Number audited										
Australia	11	4	11	4										
Cambodia	3	3	3	3										
China	104	58	45	27	19	10	29	10	2	2	9	9		
Hong Kong	5	2	5	2										
India	13	5	8	2	1	1	3	1			1	1		
Indonesia	28	20	21	15	2	1	2	1			3	3		
Japan	51	25	22	11	11	4	18	10						
Korea	46	21	33	12	1	1	11	8	1					
Lao P.D.R.	2		2											
Macau	3	1	1	1	1		1							
Malaysia	24	21	21	19	1		2	2						
Mauritius	2		2											
New Zealand	6		5				1							
Pakistan	6	4					6	4						
Philippines	22	19	14	13	1	1	6	4			1	1		
Singapore	7	3	3	3	4									
Sri Lanka	3						3							
Taiwan	27	5	13	4	6		6		1	1	1			
Thailand	30	14	26	13			2	1			2			
Vietnam	27	12	8	5	9	1	6	2			4	4		
Total Asia	420	217	243	134	56	19	96	43	4	3	21	18	0	0
Argentina	18	13	7	7	9	4	2	2						
Brazil	29	27	15	15	3	1	3	3			4	4	4	4
Canada	24	4	13	2	6		5	2						
Chile	2	2	1	1			1	1						
Colombia	5	0	5											
El Salvador	9	9	2	2	7	7								
Guatemala	4	4			4	4								
Honduras	8	8	2	2	6	6								
Mexico	36	34	14	14	15	15	7	5						
Peru	8	6	6	4	1	1	1	1						
Uruguay	1		1											
USA	38	13	18	9	3		17	4						
Total Americas	182	120	84	56	54	38	36	18	0	0	4	4	4	4

* Accessories and gear

Country	Total number of factories	Number of audited factories	APPAREL				HARDWARE*				FOOTWEAR			
			Main factories		Subcontractors		Main factories		Subcontractors		Main factories		Subcontractors	
			Total	Number audited										
Albania	2	2			2	2								
Austria	2	1	1	1			1							
Belgium	1		1											
Bosnia	1												1	
Bulgaria	7	7	1	1	6	6								
Croatia	1												1	
Czech Rep.		1							1					
Denmark	1		1											
Egypt	1	1	1	1										
Estonia	2	2	2	2										
Finland	1		1											
France	5						5							
Germany	8		1				5				1		1	
Greece	5	5	5	5										
Hungary	7	1	6				1	1						
Ireland	1	1	1	1										
Israel	4		3				1							
Italy	26	2	6	1	10		9				1	1		
Latvia	2	1	2	1										
Macedonia	3	3			3	3								
Morocco	4	7	3	6					1	1				
Poland	1	1					1	1						
Portugal	45	18	20	3	25	15								
Romania	9						9							
Russia	7	4	7	4										
South Africa	13	10	8	8			4	2			1			
Spain	2		1				1							
Sweden	2		2											
Switzerland	1		1											
Syria	3		1		2									
Tunisia	12	16	1	2	11	14								
Turkey	37	37	18	18	19	19								
UK	8	1	4	1	4									
Ukraine	2	2					2	2						
Total Europe	226	123	98	55	82	59	39	7	1	1	3	1	3	0
Total Asia	420	217	243	134	56	19	96	43	4	3	21	18	0	0
Total Americas	182	120	84	56	54	38	36	18	0	0	4	4	4	4
Total Europe	226	123	98	55	82	59	39	7	1	1	3	1	3	0
Total global	828	460	425	245	192	116	171	68	5	4	28	23	7	4

* Accessories and gear

In 2002, 460 international and local suppliers were audited, as compared to 427 in 2001.

In 2002, 56 percent of our suppliers' factories were audited. Higher coverage was not possible due to the following reasons:

- we concentrated on auditing high-risk factories and facilities with a large order volume
- factories with no order in 2002 may not have been visited
- the number of factory audits carried out by subsidiaries on behalf of the SEA team is not included in the total figure
- factories being phased out from our supply chain may not have been audited.

INTERNAL MONITORING We try to ensure that the SEA team makes an initial visit to all of our suppliers, so that we have a comprehensive picture of SOE-compliance levels and can identify common problems and solutions. Despite the growth and global coverage of the team, it is not possible to visit each facility every year. This means that although problems can be identified quickly and action plans issued to factory management, follow-up is limited. This creates special problems in factories where the management is either unwilling or does not have the capacity to make the necessary changes without on-going support.

As a result, the SEA team has a new approach to improving suppliers' performance. This involves:

- auditing factories in a more targeted way. We identify specific problem areas in factories before the SEA team carries out the audit
- moving suppliers towards independence and self-governance. In order to do this, we need to change the way we work with factories. Our plan is to shift focus from monitoring and instead provide more training to build capacity within the supply chain. In 2002, 20 percent of the SEA team's factory visits were training sessions, and 80 percent were auditing and monitoring activities. In 2003, we want to increase the number of training sessions. We plan to substantially broaden the outreach of training through capacity-building, which means more comprehensive workshops (with multiple factories) and

different levels of personnel within supplier factories

- changing how we monitor. While we will continue to conduct monitoring audits, we plan to change the nature of our monitoring and split it into two distinct types: auditing new supplier candidates; and verifying the performance of factories that receive training and go through capacity-building programmes.

FACTORY SCORING SYSTEM One of our targets for 2001 and 2002 was to implement a new factory scoring system. We have made good progress towards achieving this in 2002 but have not yet completed the project.

The new SOE scoring system is a software package that provides an effective tool to conduct audits and, at the same time, measure the level of compliance in a factory in a quick, efficient and objective manner. To do this, we need to compare performance against all the different labour and HSE standards in a meaningful way, which requires us to mark non-compliances on one scale. Developing this scale is difficult because the relative importance of different social issues is so subjective. For example, we must ask ourselves such questions as: 'is failure to comply with the wages standard worth twice as many minus marks as failure to comply with the discrimination standard?'. We are developing a protocol for this and hope to be able to roll out the new scoring system in mid-2003.

Audit coverage 2002

Region	Number of suppliers not audited yet	Number of suppliers audited in 2002 but removed from 'active' supplier list
Asia	39	96
Americas	42	20
Europe	44	15
Total global	125	131

Number of audits and training

Year	Audits	Training
2001	839	267
2002	1148*	255

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

Independent audits*

First FLA Year	August 2001 – July 2002	42 audits**
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* As part of the FLA membership

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

Employment standards /// IN 2002 WE CONTINUED TO MEASURE OUR SUPPLIERS' PERFORMANCE AGAINST THE SOE EMPLOYMENT STANDARDS AND DEVELOPED BOTH TRAINING PROGRAMMES AND RATING TOOLS AND STANDARDISED OUR ACTION PLANS. WE ALSO ADDRESSED MANY OF OUR STAKEHOLDERS' MOST PRESSING CONCERNS – CHILD LABOUR, FAIR WAGES AND LABOUR RIGHTS.

TRAINING PROGRAMMES Our training initiatives are designed to build capacity within factory management staff, so that their efforts to improve work conditions become integral to the factory's management style and sustainable over the long term.

After the launch of the Guidelines on Employment Standards in late 2001, the SEA team began training suppliers in use of the guidelines. The training sessions took place in the suppliers' own factories and in regional workshops. The guidelines set out the legal background to the standards, provide practical examples of non-compliance and suggest solutions, outline a number of case studies and provide sample documentation (such as a standard payroll template). In the context of the training sessions, this content has been translated into simple and pragmatic training modules. Similarly, the suggested solutions in the guidelines are being used as the basis to develop factory action plans where remediation of poor labour conditions is required. The guidelines are being translated into Chinese and will be available by the end of the first quarter 2003.

Sharing Best Practice meetings complement the manual-based training. The meetings, held annually throughout Asia, give factories a chance to become more aware of the progress that has been made, and the good practices that are being developed within their business. At the meetings, factories with best practices in the areas of labour, H&S and the environment are invited to share their experiences and compliance models with other suppliers. In China the local SEA staff has established a Factory SOE Sharing Club so that factories can exchange ideas and practices more regularly. Some specific supervisor training projects have been undertaken – most notably the Grow Together training project in Indonesia. The main purpose is to raise awareness of compliance issues and the needs of workers among factory supervisors and middle management. This project will be promoted in other countries throughout the Asia region in 2003.

LABOUR RATING TOOL The original version of the labour audit report document, which is completed by SEA staff when they visit a factory to check on working conditions, has been reviewed and improved. Much of the original content is still valid and forms the basis of our approach to labour issues. However, as the SOE programme has developed, it has become clear that some standards require more detailed investigation and deeper analysis. Consequently, the original labour audit report has been re-worked into a labour rating tool, and additional lines

of investigation have been included. Specifically, the tool gives greater attention to freedom of association and collective bargaining, wages and benefits, the supplier's general corporate behaviour and the extent of cooperation by its management. The tool will be field tested until October 2003.

STANDARDISED LABOUR ACTION PLAN The SEA team is now working with a standardised labour action plan. The plan is linked directly to the labour rating tool, as each section mirrors those of the rating tool both in identification of problems and solutions suggested. Following an audit, the SEA team uses their expertise and experience to judge which parts of the plan need amending or fine-tuning for a specific factory or case. The purpose of the plan is to ensure that team members do not miss any possible issues or problems, thus making sure that the information we give factories in action plans is consistent from country to country and region to region.

FAIR WAGES To define what we mean by a 'fair wage' the SOE were updated in 2001 to include a reworded clause on wages and benefits. These changes called for adidas-Salomon suppliers to gain a better understanding of the basic needs of factory workers, as well as their discretionary savings and spending patterns. While making these changes to the SOE we recognised that neither we nor our suppliers had any real data to work with, nor any standard method to determine a fair wage level. Our objective is to seek an answer to the question, raised by workers and our other stakeholders: what is a sufficient wage to cover basic needs and reasonable savings and expenditure? The second step will be to find pragmatic mechanisms to translate the answer into a workable model, to identify appropriate wage levels across all countries.

Fair wage study, Indonesia In 2001 we commissioned a local NGO, Lembaga Penelitian, Pendidikan dan Penerangan Ekonomi dan Sosial (the Institute for Social and Economic Research, Education and Information or LP3ES) to carry out a pilot study into fair wages in Indonesia. adidas-Salomon has committed to publishing the results of the study in 2003 and will host a multi-stakeholder workshop to discuss and debate the findings. To capture the widest possible range of views, the workshop will be extended to labour rights organisations, local NGOs, academics, unions, government officials and adidas-Salomon suppliers.

WORKING HOURS Working alongside sourcing departments, the SOE team continued to collect information about working hours from a large number of factories throughout 2002. The footwear factories in Asia, together with many apparel and hardware suppliers, provided monthly working hours reports. These were randomly verified by adidas-Salomon staff through interviews with workers and cross-referencing the reports with factory payroll and time records. The data and interviews reveal a trend in footwear toward greatly reduced working hours, often to below the 60-hour work week limit outlined in the SOE.

However, it is clear that working hours continue to pose one of our biggest challenges. In 2003, we will continue to research ways that working hours can be reduced while not adversely affecting wage levels. The project aims to identify the many complex causes of excessive working hours, and set out the findings in a working report. Following that, a task force within the Group will consult with factories, material suppliers, retail groups, and NGOs to map out possible solutions to the problem. Other major brands, who are working on the same issue within their own supplier base, have also provided valuable feedback on the causes of excessive working hours and possible solutions.

CHILD LABOUR During the course of 2002, adidas-Salomon continued its work on child labour through two projects: the Sialkot monitoring project, and the follow-up and assessment of the child labour education project in Vietnam.

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

Since 1997, the ILO has progressively trained and transferred expertise to a team of local monitors. These monitors now form the nucleus of a new body, known as the Independent Monitoring Association for Child Labour (IMAC), which will take forward and sustain the monitoring efforts.

As part of the programme, a local NGO assessed the education needs of Sialkot's children and devised and delivered education and training interventions, partly funded by adidas-Salomon (also see the Community involvement section on page 44).

International NGO assessment of education project, Vietnam

An education programme was established to provide young people who had been employed at a footwear factory with an education and vocational skills. An assessment of this programme was carried out by Save the Children, Sweden, through local staff and researchers who conducted broad-scale interviews with interested parties, from management and workers, to teachers and the local community. The assessment provided constructive commentary on the management of the project and highlighted areas where adidas-Salomon failed to get at the root causes of the problem. It also highlighted where a more inclusive approach could have been taken with local government education officials, the trade unions, women's groups in the area and the local community. The assessment provides a critical framework for future projects and efforts by the Group in the area of child labour. It also advocates support to local families by the employment of juvenile workers, where allowed by law, under specially controlled conditions.

MIGRANT WORKERS adidas-Salomon gave an increasing amount of attention to the plight of migrant workers throughout the industry in 2002. This issue has been highlighted through the worker interview process and our closer links with the NGO groups who monitor workplace conditions for migrant workers, a group particularly vulnerable to exploitation. We have identified a large number of migrant workers within our own supply chain, moving from Indonesia, Vietnam, the Philippines, Nepal, Bangladesh and China to relatively more developed countries such as Korea, Japan, Taiwan, Singapore and Malaysia.

While we have been developing a heightened awareness of the issue, the UN Convention on the Protection of the Rights of all Migrant Workers and Members of their Families has been the subject of serious focus and debate. On 11 December 2002, East Timor acceded to the Convention, meaning that the requisite number of ratifications was achieved and the Convention enters into force early 2003. Not only will member states be required to report on their efforts with regard to migrant workers in their countries, but suppliers and buyers who profit from the labour of migrant workers will be forced to address discrimination, under-payment of wages, excessive recruitment fees and forced labour conditions.

Monitoring migrant worker conditions, Taiwan Taiwanese manufacturers rely heavily on foreign contract workers, the majority of whom come from Thailand, the Philippines, Indonesia

and Vietnam. Numbers of these workers have recently exceeded 300,000, making the rights of migrant workers a pressing issue in these countries.

In 2002 the SEA team reviewed common problems faced by migrant workers in Taiwan that might breach the SOE or local labour laws. The result is a set of clear guidelines for the employers of migrant workers that covers placement fees, wage and benefit deductions, overtime pay, and working hours. Efforts to improve migrant worker conditions are also being developed at government level. In late 2002, the Thai and Taiwan governments signed a labour cooperation agreement aimed at improving conditions for Thai workers. adidas-Salomon's role will be to ensure workplace compliance with the agreement.

WORKER REPRESENTATION AND MANAGEMENT-WORKER COMMUNICATIONS

Throughout our training workshops and factory visits in 2002 we focused on the issue of management-worker communication. Communication and bargaining mechanisms take a variety of forms in various countries. In China, the focus has been on establishing effective HSE committees, direct management-worker discussion groups, suggestion boxes, worker magazines and counselling centres.

Towards the end of 2002, the SEA team began a process of consultation with the ILO, government manufacturing association representatives in Beijing, Chinese academics and other brands to identify ways in which worker representative groups in China might be developed within the current legal framework. We are currently exploring through discussion with NGOs and workers how the development of such organisations might be more 'grass-roots' driven. In other countries, such as Indonesia, our focus has been on projects and actions that promote multi-union coexistence in factories and proper collective bargaining processes.

Labour rights awareness in local government and the workplace, China

The development of labour intensive industries, particularly in Guangdong province, has seen a growth in labour disputes as well as an increased focus on labour safety standards in both private and state-owned enterprises. Workers often do not understand their rights and obligations within the employment relationship and are unable to find this information.

The Institute of Contemporary Observation (ICO), a local NGO, scoped a project to promote labour rights protection and assistance. Cooperation with several multi-national businesses has resulted in a user-friendly manual with information about basic labour conditions such as working hours and wage payments, industrial safety, how to report a work-related injury and claim compensation, what to do in a labour dispute, and where to go for advice. adidas-Salomon helped to set up the project and has played an important role in the development of the manual. The team assigned to the project deals with labour disputes and workers' claims on a daily basis.

Worker-management communication, El Salvador The case of an apparel factory in El Salvador demonstrates the benefit of improved worker-management communication. The factory received attention from the European media for poor health and safety practices and discriminatory employment practices. To improve the factory's treatment of workers, a solution was to develop better communication between workers and management and to involve workers in the compliance process.

The structure of the factory communication committee, including its meetings, and its elections of worker representatives, evolved substantially in 2002. There have been discernable changes in the process of creating and administering the worker management committee, with established procedures to conduct elections, institutional scheduling of meetings, recording meeting minutes, and effective communication channels between workers, committee representatives and management.

The content of these meetings originally covered topics such as planning the company's social events and organising factory sports teams. Recently the committee has identified and implemented changes that improved the quality and health standards in the factory canteen. The committee has also instituted a community donations program that identifies medical need in the local community and manages distribution of appropriate medical supplies.

Future committee activities will address continuing education and training of workers, improved feedback methods between the committee and its constituencies, and expanding the community donations programme.

Supplier scoring system

Following an audit, each factory is rated and 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.

Note to the tables on pages 36 and 39

The tables summarise the performance of our suppliers against both our labour and HSE standards. The tables use the supplier scoring system described above to compare performance.

International and local supplier factories

APPAREL

Labour standards	Asia	Americas	Europe
★	12	0	4
★★	80	7	45
★★★	132	88	144
★★★★	26	13	17
★★★★★	0	0	0
Total rated to date	250	108	210
Total rated in 2002	153	94	113
Total factories in region	299	138	180

FOOTWEAR

Labour standards	Asia	Americas	Europe
★	1	0	0
★★	1	2	1
★★★	5	3	4
★★★★	6	3	0
★★★★★	2	0	1
Total rated to date*	15	8	6
Total rated in 2002	18	8	1
Total factories in region	21	8	6

* Active factories only

HARDWARE*

Labour standards	Asia	Americas	Europe
★	2	0	0
★★	32	0	2
★★★	35	8	10
★★★★	14	6	2
★★★★★	0	0	3
Total rated to date	83	14	17
Total rated in 2002	46	18	8
Total factories in region	100	36	40

* Accessories and gear

Health and safety /// DURING THE YEAR OUR WORK ON HEALTH AND SAFETY COVERED A DIVERSE RANGE OF ACTIVITIES INCLUDING IDENTIFICATION OF HEALTH HAZARDS IN THE WORKPLACE AND INTEGRATING H&S PRACTICES INTO NEW FACTORIES. WE ALSO IMPROVED OUR TRAINING MATERIALS AND SUPPORTED SUPPLIERS IN ACHIEVING CERTIFICATION TO INTERNATIONAL STANDARDS.

APPLYING ONE H&S STANDARD ACROSS ALL SUPPLIERS

Until 2002, Asian footwear factories had dedicated SEA team H&S managers, as well as labour issues managers. As a result, SOE compliance among footwear factories received much greater attention and made more rapid progress than apparel and hardware factories. The SEA team thought that there should be one H&S standard applied to all suppliers, whether footwear or apparel. To close the gap, we organised four Sharing Best Practice meetings in 2002, bringing all adidas-Salomon factories together to share their best experiences. In the meetings, we explained to factories how to set up an H&S policy and conduct risk assessment. We hope our business partners will take the initiative now and build their own H&S management systems.

SUPPORTING SUPPLIERS' CERTIFICATION TO H&S

MANAGEMENT SYSTEMS The SEA team believes that good management systems will help factories improve their day-to-day operations. We actively encourage business partners to seek certification with internationally recognised standards such as ISO for both quality and environmental management, and OHSAS 18000 for H&S management. Selected SEA team members have to be lead auditors in order to understand how international certification schemes relate to the SOE. The SEA team also keeps in contact with consultants in the field and certification bodies, to provide support for our business partners.

IMPROVING GUIDANCE ON H&S In 2000 we launched the Health, Safety, and Environmental Guidelines to help our business partners implement H&S policy effectively. However, because we work with many different types of supplier, we found that the information in the guidelines did not meet all our suppliers' needs. To date we have therefore released 10 supplementary HSE Guidance Notes, each covering a specific topic relevant to different types of business partner.

Separate HSE Advisory Notes are also used to alert business partners to major risks, accidents or other events that may affect their business. In the case of regular reported accidents, an advisory note is sent to recommend what action is to be taken and who to contact for further information. Sometimes a note is country specific. For example, an advisory note was issued when the Occupational Health and Prevention Act in China came into force in May 2002.

Improving conditions, Asia In Asia, factories are required to report major accidents to the SEA team. This serves two purposes. First, when a report is received, the information is passed to operations staff to improve internal awareness of H&S risks. Second, the notification system allows both parties to decide whether they need any further support from the SEA team. In 2002, there were several reports of recurring fire incidents in one factory, which were mainly due to inconsistent management of H&S matters and a failure to identify and control risks. The SEA team reviewed the factory's H&S management, carried out hands-on training with the factory's SOE representatives, and conducted a joint accident investigation to find the causes and prevent recurrence.

SCOPING AN OCCUPATIONAL HEALTH PROGRAMME

Occupational health programmes have two objectives: firstly to protect workers from workplace health hazards; and secondly to promote employee health. Footwear sourcing in China was keen to roll out such a programme, in response to the Occupational Health and Prevention Act of May 2002.

In 2002, the SEA team decided to review the scope of its own efforts and guidance on occupational health and safety. As part of that we consulted with the occupational health specialist of a well-known medical service provider and a factory medical professional in order to discuss the issue.

Capacity Building Project, China This project aimed to improve the ability of NGOs and staff of footwear factories in South China to identify, evaluate and correct workplace hazards. H&S committees have been established to evaluate and improve HSE conditions. The committees are given support to enable them to develop new and safer mechanisms for workers to report problems, new processes to identify and eliminate hazards, and new systems of corporate accountability.

Occupational health and safety, China The 2001 report described our efforts to promote the use of needle guards. We initially encountered employer resistance to the programme ('it might impede the production process and reduce production rates') and workers' objections ('the needle guards get in the way'). In response to this, the SEA team created and distributed a training video in 2002 to explain how to install the needle guards and persuade both workers and management of their benefits.

In the video, four best practice factories shared their own experience of needle guards, reporting that production efficiency is not affected and that accident rates go down. In one case, needle injuries dropped from 25 percent to zero annually. The video also shows how easy it is to customise the guards for different machines, that they are inexpensive to make and most importantly, that they work. The video has proved an effective communication tool to promote the use of the guards.

Footwear industry H&S standards, Vietnam The rapidly expanding Vietnamese footwear industry already employs half a million people and is expected to continue to grow significantly. The Vietnam Business Links Initiative (VBLLI) was launched in 1999 to help the industry meet international occupational health and safety (OHS) standards. VBLLI is concentrating on the OHS issues most directly related to the footwear industry: namely the choice, storage, handling, use and disposal of chemicals used in the manufacturing process. The three-year programme is also covering electrical safety, machine guards, housekeeping and reduction of noise, fumes and dust.

The programme is supported by Britain's Department for International Development and an alliance of adidas-Salomon and two other international sportswear manufacturers. The adidas-Salomon SEA manager based in Vietnam has provided technical advice, supported the development of an OHS manual and delivered training programmes to management and staff. More than 60 percent of local footwear businesses are involved in programme activities.

INTEGRATING H&S STANDARDS INTO NEW MANUFACTURING SITES

In 2002, several adidas-Salomon business partners in Asia were planning to build new manufacturing facilities. Three large footwear factories were being built in Vietnam and two footwear factories were planned for China, one of which will employ 15,000 workers when it begins operations in 2003. The SEA team worked closely with these business partners from the conceptual design stage until actual construction, which ensured that H&S requirements were built into the new facilities. The SEA team is currently preparing a brief guide on incorporating the best HSE practices in new manufacturing sites.

WOMEN'S HEALTH In addition to monitoring the supply chain for compliance with basic H&S, specific projects in the area of women's health are taking place in a number of countries.

- In Indonesia, we have worked closely with factory-based clinic and compliance staff to develop breast-feeding programmes for the benefit of working mothers and their children.

- In Vietnam, in collaboration with the Hanoi-based Reproductive Health Information & Research Centre, the SEA team has developed materials for distribution to all Vietnam factories. The next step will be to identify local groups and health workers who could train the workforce directly, using the materials developed.

- In Cambodia, suppliers agreed to participate in the CARE programme, which delivered H&S training to a large number of workers. The training covered a range of issues, including HIV/AIDS, personal hygiene and reproduction, and work safety. Clothing manufacture accounts for 90 percent of Cambodia's export earnings, and the majority of workers are women and children. It makes the sector fertile ground for outreach health programmes aimed at these vulnerable groups.

The SEA team will work more closely with CARE in 2003 to deal with HSE training of middle management to promote acceptance of basic H&S requirements and the need for general training for the entire workforce. The training will address cultural problems between ex-pat management; mostly Chinese, and local Cambodian workers. This project will provide a model and act as a pilot for similar projects in other Asian countries, where foreign management supervises a local workforce.

- The women's health project in the Americas will be implemented in 2003, using processes learned in the Asia regional rollout. Local women's organisations in Mexico and Central America have been identified and preliminary outreach with them started in 2002.

International and local supplier factories

APPAREL

HSE standards	Asia	Americas	Europe
★	6	0	1
★★	64	7	35
★★★	155	84	161
★★★★	22	17	13
★★★★★	1	0	0
Total rated to date	248	108	210
Total rated in 2002	153	94	113
Total factories in region	299	138	180

FOOTWEAR

HSE standards	Asia	Americas	Europe
★	0	0	0
★★	4	5	0
★★★	11	0	4
★★★★	1	3	1
★★★★★	0	0	1
Total rated to date	16	8	6
Total rated in 2002	18	8	1
Total factories in region	21	8	6

HARDWARE*

HSE standards	Asia	Americas	Europe
★	5	0	0
★★	22	1	6
★★★	51	7	7
★★★★	4	6	1
★★★★★	0	0	3
Total rated to date	82	14	17
Total rated in 2002	46	18	8
Total factories in region	100	36	40

* Accessories and gear

Environmental impacts /// THERE ARE ENVIRONMENTAL IMPACTS ASSOCIATED WITH OUR PRODUCTS AT ALL STAGES OF THEIR LIFECYCLE. INCREASINGLY WE ARE SHIFTING OUR FOCUS AWAY FROM REDUCING THE IMPACTS OF OUR OWN FACILITIES, WHICH ARE RELATIVELY BENIGN, TO SUPPORTING OUR SUPPLIERS IN THEIR EFFORTS TO INTERNALISE ENVIRONMENTAL MANAGEMENT. WE ARE DEVELOPING TRAINING MATERIALS, AND SPREADING BEST PRACTICE TO HELP ACHIEVE THIS GOAL.

Although we have limited control of the environmental impacts from the manufacturing process, we aim to influence how our suppliers act. This starts with the choice of materials used to manufacture products and ends with how they are disposed of after use. Reliable facts and figures are essential to help us identify environmental impacts and to manage them properly. We have therefore been developing tools in order to provide us with accurate environmental data.

HELPING SUPPLIERS REDUCE THEIR IMPACTS During supplier and factory visits we noticed that the usual techniques to deal with environmental problems are often 'end of pipe' solutions. We believe that this approach is not effective because pollution control technology does not bring about lasting change: rather it is a short-term technical fix that is often costly to implement. We therefore favour approaches that move beyond simple regulatory compliance and promote sustainable solutions. These measures are usually directed at energy efficiency, waste reduction and pollution prevention. They save money and make economic sense – in short, they are good both for the environment and for business.

In 2002 we published Guidelines on Best Environmental Practice to support our business partners in these efforts. The guide complements the adidas-Salomon Guidelines on Health, Safety and Environment and the Guidelines on Employment Standards.

The guide describes how to tackle environmental issues in a systematic way, identifies important starting points to reduce the environmental impact of factory operations, and the benefits to be gained by doing so. To help business partners become familiar with the concepts and information presented in the guide we will run training courses on Environmental Best Practice during 2003.

INTERNATIONAL STANDARDS We consider management systems increasingly important to anticipate and meet growing social, environmental, health and performance expectations.

Well-conceived management systems can reduce waste and hence operating costs, help to gain competitive advantage and demonstrate compliance with legal obligations.

We actively encourage business partners to put in place formal HSE systems that are certified to internationally recognised standards such as OHS (OHSAS 18000) and environmental management (ISO 14001).

adidas-Salomon has already established an environmental management system for its production site in Scheinfeld, Germany. The site was revalidated under the Eco Audit scheme (EMAS II) in 2001. EMAS statements are public documents and are available on our website at www.adidas-Salomon.com

adidas Suzhou Ltd, part of our subsidiary in China, passed ISO 14001 certification in September 2002. It is being used as a 'model facility' to encourage other apparel suppliers in China to learn about ISO 14001 and implement it in their factories.

There are now three footwear factories certified to OHSAS 18000 and ISO 14001. A number of others are considering Integrated Management Systems that includes quality, health and safety and environmental management systems. Several suppliers in the Americas region gained ISO 9000 and ISO 14001 certifications in 2002. In Colombia, a supplier partner gained quality control certification, two Brazilian suppliers received ISO 14001 certifications and other partners in Mexico and Brazil were revalidated.

In 2002 we also ran several Sharing Best Practices meetings to help apparel factories introduce management systems, such as an HSE policy, risk assessment, and record keeping.

ENVIRONMENTAL INDICATORS Since 2001 our major footwear business partners have been asked to record and provide data in a survey that covers the use of raw materials, energy and water as well as the waste and emissions generated during their day-to-day activities. Our aim is to enable both adidas-Salomon and our business partners to measure and evaluate the environmental impact of their operations.

Through this exercise, our footwear business partners began

to realise that their waste can be used as raw material in other industries. Now a few of our supplier factories generate revenue by selling waste products, instead of paying to dispose of their waste.

The survey and analysis covers 14 factories in Asia (China, Vietnam and Indonesia), which together produce 95 percent of our total shoe output for the international market. The data sheet contains information on basic input data:

- infrastructure
- energy and water consumption
- the use of raw materials and operating supplies
- packing material.

and on output data:

- production volume
- generation of waste water
- generation of solid and hazardous waste.

In stage one we determined the necessary environmental data and developed relevant indicators. The first survey was conducted in the third quarter of 2001. However, the data submitted was not accurate enough to allow meaningful evaluation. We amended the questionnaire and asked suppliers to re-submit their data.

The goal of the project is not to compare suppliers with each other but to identify differences in environmental impact and to examine the causes and effects of those impacts as starting points for improvement. As a result of data analysis, several starting points for improvement have been identified. The steps for continuous improvement are:

1. defining relevant environmental indicators
2. evaluating deviations
3. verifying possible reasons
4. establishing corrective action plans.

A report documenting the findings and conclusions of this analysis will be written by mid-2003.

ELIMINATING PVC In the sporting goods industry PVC materials are most commonly used to make synthetic leathers for shoes and sports shoes, and for technical hardware such as ski boots. After reviewing and analysing the impact of PVC, and having consulted with material experts and other stakeholders, we adopted a policy in 2000 to eliminate PVC materials from our products where possible. Our target for 2002 has been to eliminate PVC from all of our spring/summer 2003 product line, except in cases where no alternative material currently exists, such as for ski boots and other highly technical products. Our reasons for replacing PVC are that:

- PVC includes a group of chemical substances called phthalates. Some phthalates are suspected of having undesirable long-term effects on aquatic environments such as seas, rivers and lakes, and of being carcinogenic in animals
- PVC contains chlorine and additives, which make it a difficult material to dispose of safely. Incinerating PVC can create hydrochloric acid as well as other types of hazardous waste

- disposing of PVC waste effectively is a costly process and would be likely to exceed the costs of incineration or depositing it in landfills. Furthermore, in many countries where our products are marketed, proper systems for the removal and recycling of PVC components do not exist.

Since none of the PVC replacement materials are as versatile as PVC, it is impossible to replace PVC with one single compound. We are therefore working with a variety of different materials to replace PVC.

Most of the PVC materials that were used in shoes or apparel have been replaced by polyurethane (PU) materials and to a limited extent by thermoplastic olefins or thermoplastic ethylene. PVC foams can be replaced with polyethylene foams, ethyl vinyl acetate (EVA) and PU foams, depending on the application. For decorative parts, we use a wide variety of materials including silicones, thermoplastic rubbers and thermoplastic polyurethane.

CONTROLLING AND MONITORING HAZARDOUS OR RESTRICTED SUBSTANCES Restricted substances cause harm or are suspected of harming human health or the environment, such as heavy metals, pesticides and ozone-depleting substances. Following consultation with testing laboratories, material suppliers and customers, adidas-Salomon has updated its existing policies and internal procedures for the control and monitoring of restricted substances.

These policies set verifiable standards that define H&S limit values for restricted substances to ensure that people can safely use our products. They follow actual legal limits as well as best practice guidelines recommended by testing institutes or consumer protection organisations such as Öko-Tex Standard 100 and various Eco-Label schemes.

Setting limits for restricted substances is only one of the important aspects necessary for developing an effective policy. It also requires clear pre-treatment analytical methods to measure a standard and to identify the material group to which the standard applies. These requirements are fundamental to ensuring that materials are tested accurately and that the test results are valid.

Material suppliers must prove that their materials comply with our standards by submitting test reports issued by external testing institutes. Development and production samples are checked randomly.

REDUCING VOCs IN FOOTWEAR FACTORIES Volatile Organic Compounds (VOCs) are found in solvents used to dissolve a product that will be applied as a layer in the manufacturing process: paints, cements, glues, and so on. Toxicity varies among different kinds of VOCs but they can all cause breathing difficulties as well as other health complaints.

Solvents are used at various stages in the manufacturing process. adidas-Salomon's policy is to reduce the solvent consumption of VOCs in our manufacturing while improving our production performance.

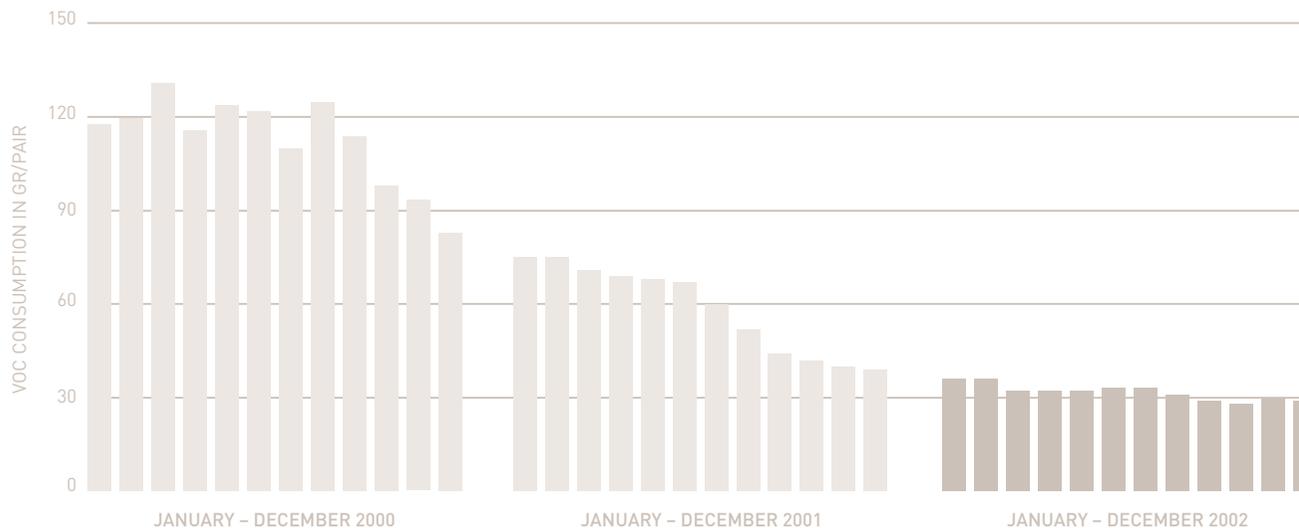
During 2002 we successfully implemented water-based alternatives to solvents in several applications, including:

- primers for some materials
- adhesives in soccer shoes using rubber outer soles
- adhesives in vulcanised shoes (for canvas materials only).

A Best Practice Manufacturing Services Manual has been written to describe the research, history, trials description,

Reducing VOCs in footwear supplier factories

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



Use of PVC in products

	% of styles free of PVC materials	Product categories where PVC is still used	Main reason for use of PVC
adidas footwear	99	Special high performance track and field shoes	No other material available to meet functional requirements
Salomon footwear	100		
adidas apparel	99	Special shirt styles with certain PVC inks	Replacement materials do not yet meet quality requirements
Salomon apparel	100		
adidas hardware (bags, balls, gloves, protective equipment)	100		
Salomon hardware (bags and gloves)	90	Special travel bags	PVC replacement in process
ALPINE			
Salomon skis and bindings	100		
Salomon boots	0		No other material available to meet functional requirements
Salomon helmets	30	Use in minor parts	Replacement of PVC in process
Salomon poles	90	Use in minor parts	No other material available to meet functional requirements
SNOWBOARDS			
Salomon boards	100		
Salomon bindings	20	Special parts of binding	No other material available to meet functional requirements
Salomon boots	20		
WINTER OUTDOOR			
Salomon skis and bindings	100		
Salomon shoes	5	Cross-country shoes	No other material available to meet functional requirements
Salomon snow shoes	50		PVC only used in minor parts; replacement in progress
IN LINE SKATES			
Salomon skates	5		No other material available to meet functional requirements
Salomon helmets	66		No other material available to meet functional requirements
Salomon protective gear	100		

process proposal, and H&S concerns of VOC reduction for each application.

For some applications, it is not possible to use cementing systems that are free of solvents. Soccer boots still use a relatively high level of VOCs as do Salomon boots. Some results have been achieved in our efforts to reduce VOC use in soccer boots and our first tests have been positive. However, more trials need to be conducted before we can consider full implementation.

The graph on page 41 shows how we reduced solvent use month by month in our three major producing countries (China, Indonesia and Vietnam). The objective for footwear products in 2002 was to reach a level 'close to 25 grams per pair'. The current achieved level is 29 grams per pair. Salomon products reached their target of 60 grams per pair.

2003 OBJECTIVE The Group's objective is to keep working on solvent elimination and to achieve a VOC level in footwear products close to 20 grams per pair by the end of 2003.

PILOT STUDY ON ENERGY MANAGEMENT This project was set up in 2001 to identify ways to use energy more efficiently in our footwear factories. By identifying and minimising waste energy through energy audits, we are aiming to reduce costs and set best performance benchmarks. The final phase of the project was completed and the final report drafted at the end of October 2002. The report suggests a number of ways to improve the efficient use of energy, some of which require capital investment, others not. If all the recommendations are followed, we estimate we can save around a million dollars.

INTEGRATED PRODUCT POLICY – PILOT STUDY In 2001, the European Commission published its thinking on Integrated Product Policy (IPP) in a Green Paper. IPP identifies environmental impacts throughout the lifecycle of products and, with stakeholder cooperation, explores solutions to these impacts that benefit both the environment and business. The strategy for IPP complements existing environmental policies.

adidas-Salomon – in partnership with environmental consultancy INTECHNICA – successfully applied to a pilot project to conduct a full lifecycle assessment of a sports shoe in 2002. The project is supported and funded by the Environmental Ministry of Bavaria.

The project will involve adidas-Salomon representatives from many different divisions and disciplines, including product management and research, scientific and market research, laboratories, material suppliers, factories, retailers and the recycling industry. The project work will focus particularly on areas such as product design, material development, material composition, energy and resources, lifespan, transport distances, product guarantee, organisation of sales and distribution.

The expected results of this project are to:

- develop methodologies, tools and systems to collect and disseminate information relevant to measuring the environmental impact of products
- establish information systems to facilitate better communication between everyone in the supply and distribution chain
- develop and market a product that has been environmentally optimised while also being fully competitive with regard to functionality, quality and price.

REDUCING THE IMPACT OF TRANSPORTING OUR PRODUCTS

The fuel used to transport goods from the country of origin to the selling markets creates carbon dioxide emissions: a major contributor to climate change. Our policy is to minimise the environmental impact caused by transporting goods. Air freight creates the most emissions so we have a target to reduce shipments by air freight to below 2001 levels.

In 2002 we did not achieve our target. A contributing factor to this was to quickly react on unexpected customer requests during the soccer World Cup, resulting in shortened lead times for the delivery of our products. Another reason was our suppliers' response to increased safety concerns. This led to the relocation of some of their operations, resulting in an increase in air shipments.

How adidas products are transported*

	2002	2001	2000
FOOTWEAR			
Truck	4	3	3
Sea freight	94	96	94
Air freight	2	1	1
Sea and air freight	0	0	1
APPAREL			
Truck	32	32	26
Sea freight	62	64	63
Air freight	5	4	9
Sea and air freight	1	0	2
HARDWARE**			
Truck	7	5	8
Sea freight	86	92	89
Air freight	7	3	3
Sea and air freight	0	0	0

* Figures expressed as a percentage of the total number of products transported

** Accessories and gear

Community involvement /// ENLIGHTENED BUSINESSES RECOGNISE THEY HAVE A CONTRIBUTION TO MAKE TO THE COMMUNITY WHERE THEY OPERATE THAT GOES BEYOND EMPLOYING LOCAL PEOPLE. A THRIVING COMMUNITY WILL HELP CREATE THE ENVIRONMENT FOR A SUCCESSFUL BUSINESS. WE HAVE SELECTED ONE COUNTRY THAT ILLUSTRATES OUR INVOLVEMENT WITH THE LOCAL COMMUNITY, PAKISTAN, WHERE WE HAVE A LONG HISTORY OF SUPPLIER PARTNERSHIPS. THIS IS ONLY PART OF THE FULL STORY OF OUR CONTRIBUTION TO LOCAL COMMUNITIES, AND WE ARE COMMITTED TO REPORTING THIS MORE COMPREHENSIVELY IN FUTURE REPORTS.

COMMUNITY SUPPORT IN SIALKOT, PAKISTAN adidas-Salomon has sourced footballs from the Sialkot area of Pakistan for the past 27 years. Over that period it has grown from a traditional cottage industry to one with a more formal manufacturing structure, with centralised production of the ball components and dedicated stitching centres where the balls are assembled. A major driver for this change was the NGO-led child labour campaigns in the mid-1990s, which highlighted the use of underage workers in poor rural communities. The campaigns served as a wake-up call for adidas-Salomon and a clear message that we had to address our responsibilities to our suppliers more comprehensively. As a consequence, improved production tracking and monitoring systems were introduced.

In parallel with our internal efforts, adidas-Salomon joined other major brands, the World Federation of Sporting Goods Industry, local suppliers and community groups, and international NGOs, such as Save the Children, in supporting the formation of an independent child labour monitoring programme in Sialkot. This came into being in February 1997 when the ILO, UNICEF and the local Sialkot Chamber of Commerce and Industry (SCCI) signed a partner agreement to prevent and eradicate child labour from the football manufacturing industry in Pakistan.

The independent monitoring programme required suppliers to register formally the locations used for football stitching, which would then be visited by ILO monitors. This spurred the development of larger purpose-built stitching centres that, due to local custom and culture, were male-only. Women who had previously stitched balls at home in their villages were therefore deprived of an important source of income. To address this, adidas-Salomon has actively encouraged the development of smaller village-based stitching units, where women can work together and earn an income for their families. To date, 17 such stitching units have been established by our suppliers, providing employment for over 1,100 rural women.

To combat child labour and bring about long-term and lasting change, the football stitching industry in Sialkot has required not just preventative measures, but also independent external monitoring. The monitoring body formed by the ILO, UNICEF and SCCI has sought to address the root causes of the

problem, and has worked in partnership with a range of local organisations and industry bodies to raise awareness and provide social protection and education for local children. adidas-Salomon has contributed to this through the direct funding of an education programme run by Sudhaar, a local NGO. Sudhaar has focused its efforts on improving the quality of education in schools located in those villages where there is a high concentration of football stitching families. The education programme, which was launched in February 1998 in partnership with Save the Children UK, has proved to be very successful. Achievements to date include: reorganising 125 school councils; providing 300 teachers with teacher training and improving the infrastructure of 105 schools.

SUPPLIER SUPPORT FOR THE LOCAL COMMUNITY In addition to their efforts in eliminating child labour, our main suppliers in Sialkot have made other contributions to their local community. In cash terms these contributions regularly exceed one million rupees each year. Often working with local NGOs, our suppliers have supported:

- local education projects such as subsidising the costs of children attending school
- social welfare initiatives such as financial support for hospitals or widows
- urban infrastructure projects such as funding road-building and sewer construction
- employee benefits such as subsidising meals and clothes or providing interest-free loans.

COMMUNITY INVOLVEMENT, NEXT STEPS Our SOE state that adidas-Salomon favours business partners who make an effort to contribute to their local communities. We have not, however, sought to measure this as a formal area of compliance. From 2003 we will begin to collect information on the community involvement and charitable activities of our suppliers, and look for ways to link our suppliers' efforts with our own. Also, by the first quarter of 2003, we will have in place a formal policy on charitable donations and corporate giving by adidas-Salomon Group companies.

The journey ///

The journey

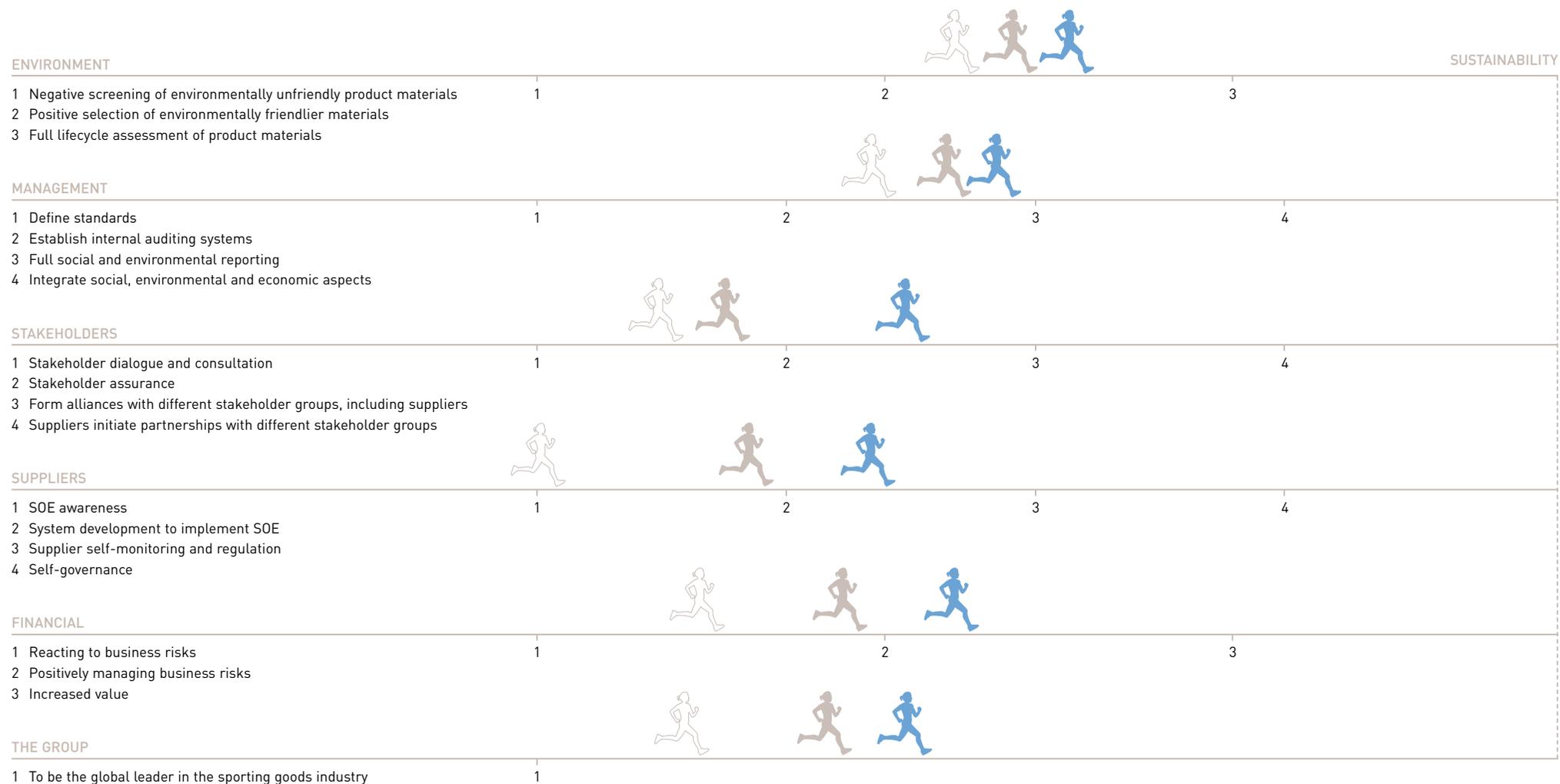
The six inter-linked roads on the journey to sustainability and strong governance are shown below. Our 2000 performance is shown as the outlined runner, with 2001 as the gray runner. The blue runner shows our performance in 2002.

Progress against targets

Progress against targets on page 46–47 summarises all the targets we set for 2002. 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 2003

Our targets for 2003 are listed on page 48.



Progress against targets ///

Targets for 2002	Actual performance	0	10	20	30	40	50	60	70	80	90	100%
ENVIRONMENT To reduce VOC-solvent level from less than 40 grams to around 25 grams per pair of shoes	Solvent consumption was reduced to 29 grams per pair for adidas footwear, and to 60 grams per pair for Salomon. Certain Salomon footwear styles have not achieved the targets.											
To establish a metric system to measure the environmental impact of footwear manufacturing at production sites	Environmental data were submitted by footwear factories operating in China, Indonesia and Vietnam for 2001 and 2002. The data were analysed and a metric system was formed following this. Results and conclusions will be reported to factories and management in the first half of 2003.											
To launch the Guidelines on Best Environmental Practice to accompany the Guidelines on Health, Safety and Environment and the Guidelines on Employment Standards	The Guide to Best Environmental Practice was launched in October 2002.											
Complete elimination of PVC materials by spring/summer 2003 from product models where PVC is still in use (except ski boots and a few highly technical products)	adidas and Salomon soft goods are now almost completely PVC-free. Certain Salomon hard goods (ski boots and highly technical products) still contain PVC components due to a lack of acceptable replacement materials (see page 42).											
To start a pilot project and case study based on principles of integrated product policy	A project outline has been developed and submitted to the Bavarian Ministry of Environment. The project outline has been approved, the steering committee formed and the work schedule developed. We intend to roll out the project in 2003 and 2004.											
MANAGEMENT To hold 300 SOE training sessions	255 SOE training sessions have been held. Multiple training workshops were held in Asia with more than one factory participating, compared to last year where training was generally given to one factory at a time.											
To have a consistent corporate approach to supporting and funding community programmes	A corporate giving and donations policy has been drafted. It will be finalised and implemented in 2003.											
To integrate social and environmental affairs further into the mainstream of the Group through systems development, awareness raising and stronger links between the regional SOE programs	Better integration has been achieved within sourcing and operations. There has been increased SOE impact on the product allocation process, and more involvement in supplier selection. Various internal HR-sponsored awareness raising sessions for new and current employees were held. We organised SEA / SOE orientations for management of other adidas-Salomon brands, licensees and subsidiaries. We posted reports, statements and other key documents on our website. We will continue to work to integrate further SEA into the mainstream of the Group.											

Targets for 2002

Actual performance

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

SUPPLIERS

To have 10 percent of adidas international suppliers independently audited by FLA-accredited monitors in the period from 1 August 2001 to 31 July 2002, and to comply with new FLA guidelines thereafter.

42 independent audits have been conducted between August 2001 and July 2002, which covered approximately 10 percent of our international supplier base. The target set by the FLA was five percent. adidas-Salomon is fully compliant with all new FLA requirements.



To assess all international suppliers using the computerised factory scoring system that will be introduced in the second quarter.

A more detailed rating system delivering quantitative performance data has been developed and was field-tested for three months in 2002. An HSE rating system has been defined; due to the complexity of the labour rating tool it has not been finalised yet. The HSE and labour rating tools will be rolled out together.



To complete a study of workers' wages and benefits in Indonesia.

Survey work and initial reporting has been completed. Draft report is currently being reviewed and will be finalised in first half of 2003. An independent reviewer has been appointed.



To organise structured stakeholder dialogue in Europe and the USA.

Completed dialogues in Asia, the Americas and Europe.



FINANCIAL

Our expectation is to increase Group sales by at least 5 percent, with double-digit growth in both North America and Asia.

Sales grew seven percent to reach record level of 6.5 billion euros



To maintain our gross margin within our long-term range of 41-43 percent.

Gross margin reached 43.2 percent.



To improve on working capital by turning inventories faster and improving customer payment terms.

Inventories reduced by seven percent, receivables up less than sales growth, aging improved.



We anticipate delivering earnings growth of 5-10 percent.

Earnings grew by 10 percent.



THE GROUP

To strengthen our brands and products continuously in order to improve our competitive position and financial performance.

In 2002, new products were launched by all brands in all major markets. In addition, major sporting events, in particular the World Cup and Olympics, helped drive stronger brand awareness and financial results in 2002.



Targets for 2003 ///

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.
- To reduce further the use of hazardous chemicals in the manufacture of hardware in accordance with international standards.
- To provide a progress report about improved measurement of environmental impact.
- To develop a strategy to extend the use of organically grown cotton for apparel products.
- To provide a progress report about the pilot project and case study based on principles of integrated product policy.



MANAGEMENT

- To provide 100 specific training sessions to build capacity in suppliers' factories.
- To further enhance relationship to sourcing operations through system development and participation in key initiatives.
- Increase employee awareness of the Group's social and environmental programmes.
- To conduct regional stakeholder dialogues and focused group discussions in each region – the Americas, Asia and Europe.



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.
- At least 12 factories in the supply chain will 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.
- Fully use the computerised rating systems for factory audits and develop appropriate databases and analytical techniques to assess the results.
- 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.
- Complete the fair wages pilot study and run a multi-stakeholder workshop to discuss the findings.



COMMUNITY INVOLVEMENT

- To finalise and execute a corporate approach to fund and support community programmes.
- To survey suppliers in order to obtain an overview of the level of community involvement.
- To more effectively report on community involvement in 2003 report.



FINANCE

- Increase Group sales by around five percent.
- Deliver double-digit currency-neutral sales growth in Asia and North America.
- Deliver a gross margin of 42-43 percent.
- To deliver earnings growth at a higher rate than 2002.
- Maintain and develop shareholder confidence.



About this report and 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 beyond 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.com

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* 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.

Glossary ///

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 setting and helping to verify standards for labour and HSE performance.

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

HSE Health, safety and environment.

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

ISO 14000/1 Environmental management standard.

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

Non-governmental organisations (NGOs) Campaigning groups 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 but 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 with all the people who have an interest in the company (stakeholders) in a structured way, in order to understand their concerns and respond appropriately.

Standards of Engagement (SOE) A set of labour, health and safety, and environmental principles. The standards are designed as tools to help adidas-Salomon choose supply partners, monitor their performance and identify problems.

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.

Contact us ///

For further information please contact:
adidas-Salomon
World of Sports
Social and Environmental Affairs
91074 Herzogenaurach
Germany
Telephone: +49 9132 84 0
Facsimile: +49 9132 84 3242
Email: sustainability@adidas.de
Website: www.adidas-Salomon.com

Credits ///

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