



GROUP MANAGEMENT REPORT

OUR COMPANY

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CORPORATE STRATEGY

Everything we do is rooted in sport. With sport playing an increasingly important role in more and more people's lives, on and off the field of play, we operate in a highly attractive industry. Through our authentic sports brands, we push the boundaries of products, experiences and services to drive brand desire and capitalize on the growth opportunities in sport as well as in sports-inspired casual and activewear.

OUR CORE BELIEF: THROUGH SPORT, WE HAVE THE POWER TO CHANGE LIVES

The importance of sport, however, goes far beyond that. Sport is central to every culture and society and is core to an individual's health and happiness. Therefore, we believe that, through sport, we have the power to change lives. And we work every day to inspire and enable people to harness the power of sport in their lives.

OUR MISSION: TO BE THE BEST SPORTS COMPANY IN THE WORLD

It is our mission to be the best sports company in the world. Best means that we design, build and sell the best sports products in the world, with the best service and experience, and that we do so in a sustainable way. Best is what our consumers, athletes, teams, partners, media and shareholders will say about us. We are confident that we will see improvements with regard to market share, leadership and profitability once people are saying that we are the best.

STRATEGIC BUSINESS PLAN: CREATING THE NEW

'Creating the New' is our strategic business plan until the year 2020. Our ambition to further drive top- and bottom-line growth by significantly increasing brand desirability builds the core of Creating the New. The strategic business plan therefore focuses on our brands as they connect and engage with our consumers. This consumer-centric approach is

driving significant improvements in the desirability of our brands and has increased our relevance with consumers around the globe. As a result, we are gaining market share in those categories, markets and cities that we have identified as future growth drivers for our company.

STRATEGIC CHOICES

Our strategic business plan has a powerful foundation in our unique corporate culture and is built around three strategic choices that will support us in intensifying our focus on our consumers and will drive brand desirability: Speed, Cities and Open Source.

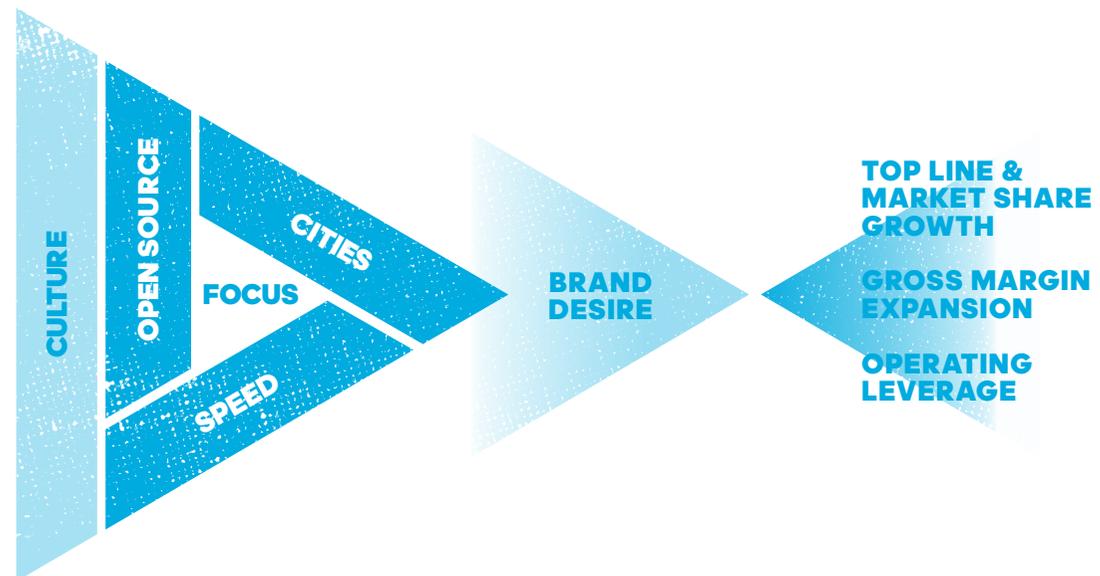
Culture

We have great talents in our organization who work with passion for sports and our brands. Our people will bring our strategy to life and our culture will make the difference in achieving our long-term goals. We are convinced that a culture of creativity, collaboration and confidence will be a key enabler for us to Create the New. [SEE PEOPLE AND CULTURE, P. 81](#)

Our leaders role model this behavior. To enhance our leadership structure, we established the Core Leadership Group at the end of 2016. This selected group of leaders is mainly responsible for driving the execution of our strategic business plan, with a particular focus on improving cross-functional collaboration and decision making. In 2017, we

Our strategy: 'Creating the New'

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continued to sharpen our leadership structure by adding an Extended Leadership Group which supports the Core Leadership Group in implementing our strategy and which will serve as a succession pipeline for Core Leadership Group members. The Leadership Framework, introduced in 2017, unites all leaders in our company through a clear definition of what strong leadership looks like at adidas.

We believe that a performance culture is essential to successfully executing our strategy. To further promote a performance culture within our company, we have finalized a new way of developing our people and evaluating their performance. In addition, we made major progress in recalibrating our approach to compensation and benefits. Long-term remuneration for our senior management, for instance, will be simplified and linked to the development of the company's bottom line and our share price going forward in order to further align the interests of our senior leaders with the interests of our shareholders.

As a company, we value diversity and promote inclusivity. While today our employee base is already very diverse in terms of nationalities, we also aim to continuously increase the share of females in leadership positions. With the appointment of Karen Parkin to the Executive Board in May 2017, we have made further progress in this regard. In addition, between July 2015 and June 2017, the share of women at Board-1 level increased from 11% to 18%, and at Board-2 level the percentage of women grew from 26% to 29% during the same period. [SEE PEOPLE AND CULTURE, P. 81](#)

Speed

Driving brand desirability begins with putting our consumers at the heart of everything we do and serving them in the best possible way. This involves ensuring that consumers always find fresh and desirable products where and when they want them and with an unrivaled brand experience. This, in turn,

means to us being able to anticipate what consumers want and reacting accordingly in a timely manner. Being fast will give us a decisive competitive advantage. The benefits include higher product availability, reduced inventory risk, incremental net sales and higher margins. Speed is therefore a critical and powerful lever for us.

We are using our industry-leading experience to further evolve our entire business model end-to-end, from range planning to product creation, sourcing, supply chain, go-to-market and sales. In this context, our Speed concept builds on three programs:

- **Never out of stock:** We strengthen our existing 'never-out-of-stock' business proposition by setting a global, permanent offer with longer life cycles and continuous reproduction and replenishment. This ensures our most iconic and desired products are permanently available to our consumers.
- **Planned responsiveness:** Systematically monitoring trends at the point of sale enables us to better read demand signals, re-order seasonal products on shorter lead times and deliver them within the season. By doing so, we can repeat seasonal product successes and fulfil higher consumer demand than initially forecast.
- **In-season creation:** We create ranges later in the season to ensure we capture the latest trends in our industry. This, in turn, helps us to create unexpected newness and drive brand desire.

Since the launch of the Speed programs, we have steadily expanded the coverage. All categories and markets have now been fully onboarded and started to capitalize on the benefits of the Speed programs. The net sales share of speed-enabled products has continuously increased to a level of 28% in 2017 which is fully in line with our overall ambition to increase the share of speed-enabled products to at least 50% by 2020. In addition, we are making further progress to achieve a 20%

higher share of full-price sales with this part of our business compared to the regular range.

In addition to focusing on Speed in our existing supply chain and production processes, we also explore new, disruptive business models and technologies to make us faster. At the end of 2015, we opened our first *Speedfactory* [SEE GLOSSARY](#) in Ansbach, Germany. Using smart manufacturing instead of centralized production, it brings production closer to where the consumer is. It opens doors to the creation of products completely unique to the fit and functional needs of our consumers, through a combination of the craft of shoemaking and cutting-edge technology. 2017 saw the first major product to be created at the Speedfactory: The AM4 series, an individually designed and manufactured shoe made for our global key cities, went into production. In addition, we opened a second Speedfactory in Atlanta, USA, to create product more quickly for and closer to the US consumer. Bringing the two factories up to speed is what we are focusing on in 2018. And while Speedfactory enables us to rethink conventional manufacturing processes, it also enables us to continuously learn from it, which in turn will help us to also improve efficiency and increase opportunities within the traditional supply chain, which will remain the backbone of our global sourcing activity.

[SEE GLOBAL OPERATIONS, P. 74](#) [SEE INNOVATION, P. 78](#)

Cities

Urbanization continues to be a global megatrend. Most of the global population lives in cities and already today cities account for around 80% of global GDP. Cities are shaping global trends and consumers' perception, perspectives and buying decisions. To be successful in the future, we therefore need to win the consumer in the world's most influential cities. We have identified six global megacities in which we want to over-proportionally invest to grow share of mind, share of market, share of trend: London, Los Angeles, New York, Paris, Shanghai and Tokyo.

We aim to deliver extraordinary experiences to consumers in these cities across all touchpoints by engaging more deeply with them in communities where they live, places where they work, fields, courts and streets where they play and doors where they shop. At the same time, we strive to create high synergies between our activation and commercial efforts. This also includes aligning our initiatives with similar activities of key retail partners.

It is our goal to create an end-to-end ecosystem in these cities which connects consumers to relevant products, through bottom-up activation and holistic retail experiences:

- **Activation:** Our global key cities offer a unique platform to activate our brands. Key successes in 2017 include the ‘Green Light Run’ in Tokyo, receiving six Cannes awards, as well as the Parley ‘Run for the Oceans’ in New York City and the launch of our new football footwear franchise Nemeziz in London, which have not only created brand heat in the respective cities but also received significant global social media coverage.
- **Products:** We continue to drive a multi-pronged strategy of product introductions, focused across all six cities, including global campaign launches and exclusive collections. With the launch of the AM4 series in 2017, we introduced the first shoe that was co-created with consumers from our global key cities and tailored to their unique demands. Produced in our Speedfactory, the AM4 saw its debut in London and Paris at the end of 2017, with the remaining four global key cities to follow in 2018.
- **Experiences:** We are committed to providing premium retail experiences to our consumers with executions that connect, engage and inspire them. The opening of our second adidas Originals flagship store in London in 2017 set a new benchmark in the industry. Moreover, in collaboration with our retail partners, we made significant progress in transforming retail spaces into premium shopping spaces in key doors within key trade zones.

The 2017 results for several KPIs (NPS and market share) signal we are well on track to achieve our long-term target to double revenues in our global key cities by the end of 2020 compared to 2015. Our global cities make an above-average contribution to the overall growth of our company and help us achieve market share gains. In addition, we also experienced a relative improvement in brand desire in most of our key cities.

Open Source

Open Source is a collaboration-based innovation model that aims to build brand advocacy by opening the brands’ doors to the consumer and by inviting him or her to co-create the future of sport and sports culture with us. It is about learning and sharing, about starting conversations between the brand, external experts and consumers and about giving them the chance to have an impact on what we do. We provide access for externals to tools and resources we use to create, thereby acquiring and nurturing creative capital, and explore new territories so as to create unprecedented brand value for the consumer beyond mere transactional businesses.

We have defined three strategic initiatives for Open Source:

- **Creative collaborations:** Creative collaborations increase our creative capital through new tools, new environments and new perspectives from outside creative thinkers. They are meant to give creativity a platform and provide the right tools for ideas to blossom. With the Brooklyn Creator Farm, for example, a design space and creation hub, we offer urban creative talent a platform and invite them in to fuel innovation in sport with their ideas, outside any regular seasonal product creation calendars. Following the initial set-up phase in 2016, the creator farm has meanwhile started to have a visible impact on our creative direction and leaves a footprint in the local creative community. In addition, we have evolved our successful

creative partnerships with Alexander Wang, Kanye West and Stella McCartney, among others, to further drive brand desire and growth.

- **Athlete collaborations:** Through athlete collaborations we aim to build communities of athletes that help shape the future of their sport together with us. Such collaborations include relationships with the world’s best athletes and teams, but they also take place on a local level. To directly engage and interact with a broader consumer community, we have expanded our digital and physical space projects in 2017. For instance, ‘adidas runners’, a highly engaged community of runners, now counts over 50,000 active runners in Western Europe alone. Other collaborations include Wanderlust, a producer of the largest yoga lifestyle events in the world, or our Tango League, a grassroots event for the football enthusiast, among others.
- **Partner collaborations:** The strategic initiatives in the area of partner collaborations intend to open up our knowledge of sport by working with the best in other fields. By exchanging core competencies, we will create unique value for our brands and ultimately also for our consumers. Our partnership with *Parley for the Oceans* [SEE GLOSSARY](#) serves as a prime example. As a founding member of the organization, our support goes far beyond financial aid to fund beach clean-ups. In 2017, we launched multiple franchise silhouettes, such as the UltraBOOST, NMD or EQT, made out of *Parley Ocean Plastic* [SEE GLOSSARY](#). In total, we have produced more than one million pairs of shoes using Parley Ocean Plastic. [SEE SUSTAINABILITY, P. 88](#) In addition, we joined forces with Carbon, a company pioneering in the field of 3D printing, to launch a new product and platform: Futurecraft 4D. Driven by athlete data, a production process called ‘Digital Light Synthesis’ enables us to print previously impossible designs without labor-intensive and complex assembly. The Futurecraft 4D shoe launched in 2017 and will be expanded in the course of 2018. [SEE INNOVATION, P. 78](#)

We remain committed to embedding external creative capital in our processes to extend our possibilities in creating the future of sport. To ensure that we are at the pulse of the consumer journey at key moments and touchpoints in their lives, we have identified two key targets which we are progressing against: On the one hand, we aim to drive brand heat by inviting consumers to become part of our creative culture, thereby measuring the user-generated content on social media, and on the other hand to grow the number of users in our digital ecosystem. For both targets, we made considerable progress in 2017. By using the insights we generate through Open Source, we will craft better products and services for our consumers, driving improvements in brand desire, sales, market share and profitability.

'CREATING THE NEW' ACCELERATION PLAN

In March 2017, we introduced a number of initiatives to foster brand momentum and accelerate top- and bottom-line growth:

Portfolio

Every entity must contribute to the success of our company, be it a brand, a channel or a market. We constantly revisit the performance and strategic fit of our portfolio, now with a narrowed focus on operating within our core strength areas of athletic footwear and apparel. This will allow us to reduce complexity and pursue our target consumer more aggressively with both the adidas and the Reebok brand. In 2017, we completed the sale of the TaylorMade, Adams Golf and Ashworth brands as well as our CCM Hockey business. In addition, we continued to execute upon Reebok's turnaround plan 'Muscle Up', aimed at accelerating the brand's top-line growth and improving its profitability.

adidas North America

North America represents the biggest market in the sporting goods industry with a total share of approximately 40%. At the same time, from a geographical perspective, North America

represents the biggest opportunity for the adidas brand, given its relatively small market share compared to other regions. To improve the adidas brand's overall positioning in the region, we have made North America a strategic priority and started to significantly increase our investments into North America in order to be more relevant and always visible to the consumer. In this context, over the last years, we have stepped up investments into our organizational set-up, including the further expansion of our US headquarters in Portland, elevated our marketing efforts and upgraded our distribution infrastructure. As a consequence of those initiatives, North America saw strong double-digit top-line growth in each of the past three years, despite an increasingly challenging and promotional environment. While we are pleased with the progress we have been making in North America in recent years, we are still not satisfied with our current position, which leaves significant upside for the years to come. Therefore, going forward, we will continue to execute our game plan for North America in order to continue to increase our market share and reach our target of € 5 billion in revenues for the adidas brand by 2020. North America, however, is more than just a market share story, as our profitability in the region remains below our global profitability level even after significant improvements in 2017.

ONE adidas

We continuously strive for operational excellence. ONE adidas encompasses a set of initiatives that will enable our company to work smarter, more efficiently and in a more aligned way. By focusing on three pillars – *Brand Leadership* [SEE GLOSSARY](#), marketing effectiveness and operating efficiency – we challenge the current standards and norms in our organization. In order to create a more scalable business model, we will therefore focus on those opportunities that enable us to standardize and harmonize current processes and procedures. In this context, 2017 saw the kick-off of several initiatives which will significantly improve our

operating efficiency and profitability in the years to come, and disciplined execution has yielded some first positive results already. For example, we achieved a further reduction of our product range and marketing concepts. This not only has a positive impact on profitability but also increases the impact of our product franchises. Similarly, we carried out major simplifications on the material, packaging and production side, which helped us to realize an increase in product margins. Our pipeline of initiatives aimed at enabling scalability and operating leverage is filled and we expect more benefits to flow through in the years to come.

Digital

The digital transformation is fundamentally changing the way our consumers behave and the way we work. Technology has enabled us to accelerate building direct relationships with our consumer. Improving digital capabilities along the entire value chain enables us not only to interact with the consumer, but also to become faster, better and more efficient in every part of the organization. In 2017, we established the 'Digital Leadership Team' with the purpose to orchestrate the digital initiatives across the company and support functional teams in decision making. In collaboration with the Executive Board, the Digital Leadership Team has defined a clear roadmap of digital priorities. In this context, our own e-commerce sites adidas.com and Reebok.com are our biggest and most important stores, which enable growth by delivering a unique consumer experience that is premium, connected and personalized. To support our 2020 own e-commerce revenue target of € 4 billion, we went through a major paradigm shift in 2017 in how we gear and align our activities towards digital. As we continuously improve our digital capabilities in order to serve our consumer in the best possible way, in 2017 we introduced new features and technologies on our online platform to improve the shopping experience. In addition, 2017 saw the launch of the adidas shopping app with more than 600,000 downloads in less than two months. With 57%

growth, our e-commerce platform was by far the fastest-growing channel in 2017.

FINANCIAL AMBITION UNTIL 2020

Creating long-term value for our shareholders drives our overall decision-making process. Therefore, we are focused on rigorously managing those factors under our control, making strategic choices that will drive sustainable revenue and earnings growth and, ultimately, operating cash flow. We are committed to increasing returns to shareholders with above-industry-average share price performance and dividends. [SEE INTERNAL MANAGEMENT SYSTEM, P. 102](#)

Our unique corporate culture and the three strategic choices will continue to be step-changers with regard to brand desirability and brand advocacy. In combination with the initiatives that are part of our acceleration plan, this will enable us:

- **To achieve top-line growth significantly above industry average:** We aim to increase currency-neutral revenues annually between 2015 and 2020 at a rate between 10% and 12% on average (initially, in March 2015: high-single-digit currency-neutral increase).
- **To win significant market share across key categories and markets:** We have defined key categories within the adidas and Reebok brands that will spur our growth going forward. From a market perspective, we have defined clear roles for each of our markets, depending on macroeconomic trends, the competitive environment and our brand strength in the respective markets.
- **To improve our profitability sustainably:** We plan to substantially improve the company's profitability, growing our net income from continuing operations by an average of between 22% and 24% per year between 2015 and 2020 (initially, in March 2015: increase at around 15%; updated in March 2017: increase between 20% and 22%).

- **To deliver on our commitment to increase shareholder returns:** Creating the New includes a strong commitment to generating increasing returns for our shareholders. Given our firm confidence in the strength of the company's financial position and future growth ambitions, we target a consistent dividend payout ratio in a range between 30% and 50% of net income from continuing operations.

ADIDAS BRAND STRATEGY

MISSION: TO BE THE BEST SPORTS BRAND IN THE WORLD

The adidas brand has a long history and deep-rooted connection with sport. Its broad and diverse sports portfolio, from major global sports such as football and running, to regional heartbeat sports such as American football and rugby, has enabled the brand to transcend cultures and become one of the most recognized and iconic global brands, on and off the field of play. The adidas brand's mission is to be the best sports brand in the world, by designing, building and selling the best sports products in the world, with the best service and experience.

Driven by a relentless pursuit of innovation as well as decades of accumulating sports science expertise, the adidas brand has developed a truly unique and comprehensive sports offering. Spanning footwear, apparel, equipment and services, the brand caters for all, from elite professional athletes and teams to any individual who wants to make sport part of their lives. We help athletes of all levels to make a difference – in their game, in their lives, in their world. This is anchored in our core belief that, through sport, we have the power to change lives.

CONSUMER OBSESSION: CREATING FOR THE CREATORS

The consumer is at the heart of everything the adidas brand does. By constantly developing desirable products and inspiring experiences, the brand strives to build a strong image, trust and loyalty with consumers. Through 'Creating the New', the adidas brand has refined its strategic direction, operational processes and incentive systems, to foster a culture of consumer obsession across its entire organization.

— **Operating model:** To ensure long-term success, it is important that we continue to challenge ourselves to learn and grow. We must constantly iterate to become faster and

stronger. Therefore, the adidas brand continues to evolve directed by the guiding principles of *Brand Leadership* [SEE GLOSSARY](#), our operating model. The aim of Brand Leadership is to provide an organizational structure which enables a 'consumer-obsessed' culture that can act with speed, agility and empowerment. In 2017, to further strengthen collaboration and alignment in execution across the sport-specific categories, we combined all of the sport-specific business units under one leadership. Similarly, we have created a new business unit called Core, which caters to the value consumer across categories. Moreover, to simplify the interaction between global and local organizations, we consolidated Brand Management and Concept-to-Consumer into a holistic marketing function. Finally, to streamline and align the two most future-facing functions, we consolidated Creative Direction and our Future Team to create continuity and creative fidelity stretching from upstream innovation, engineering and sports science through future design, advanced design, brand design and seasonal creative direction.

— **Creator archetype:** Owing to the rapid evolution of sport and sports culture, the adidas brand targets key consumer groups and influencers to create brand desirability and momentum through a well-defined consumer segmentation strategy. The consumer grid comprises six key quadrants (Male Athlete, Female Athlete, Young Creator, Streetwear Hound, Amplifier and Value Consumer), which are not mutually exclusive. Within this grid, it is key to win the most influential consumers, defined as the creator archetype. True to the brand's values, these influential consumers define themselves as a work in progress – are all doers and makers, first to adopt, focused on what's new and what's next. A large portion of creators live, play and work in the world's most influential and aspirational cities, a key reason for the company's Cities strategic choice. In 2017, the adidas brand accelerated global and local marketing initiatives to amplify the brand's creator positioning in the marketplace.

— **Consumer centricity:** Companies that put the consumer's voice as a centerpiece of their decision-making process have proven higher levels of success in creating brand advocacy. Therefore, we implemented a global Net Promoter Score (NPS) ecosystem in order to drive brand momentum in a measurable and objective manner. NPS, first introduced in 2015, has become an important part of the adidas brand's advocacy program. Through this program, we strive to understand consumers' perception (positive and negative) of the brand and the key drivers which motivate them to recommend the brand to their friends. [SEE INTERNAL MANAGEMENT SYSTEM, P. 102](#)

PRODUCT FRANCHISES: CREATE THE MOST DESIRED SYMBOLS IN SPORT

We are convinced that footwear has the highest influence on brand perception among product categories. Footwear is also the most powerful driver of NPS, which in turn translates directly into consumer purchase intent and our potential to grow market share. Therefore, the adidas brand is focused on relentlessly creating newness in footwear, as a function of cutting-edge technological innovation with references to history, drawing from deep knowledge and an archive which are unrivaled in the industry. At the same time, the brand has a clear strategy to reduce the number of footwear models, putting a stronger focus on key franchises that can really make a difference for the brand. Such footwear franchises are defined as long-term concepts that we commit to for a multi-year period. The goal of franchises is not only to shape sport, but also to influence culture. They are built to create trends, rather than follow. They are targeted directly at the consumer through iconic features, stories and functions, and have the potential to be iterated and expanded over time. Their life cycles are being carefully managed, to ensure longevity. In addition, franchises will be prioritized throughout the value chain, building on the company's strategic choices of Speed, Cities and Open Source. The adidas brand expects its top

footwear franchises to represent at least 30% of the brand's footwear business by 2020. In 2017, key adidas brand franchises included modern icons such as the UltraBOOST, PureBOOST, Alphabounce, 'X', Nemeziz, NMD and EQT as well as a blend of past icons such as the Superstar, Stan Smith and Gazelle.

Following on from the strong success in footwear, in 2017 the adidas brand started to extend its franchise methodology and approach to apparel. Focused on a set of initiatives that have proven to be successful in footwear, the brand aims at accelerating its performance in apparel going forward. In this context, 2017 saw the successful evolution of the Z.N.E. Hoodie as part of the new Athletics apparel product line. The Z.N.E. Hoodie, specifically engineered to remove distractions and maximize athletes' focus in the make or break period before they compete, was succeeded by the Z.N.E. pants and a suite of related apparel products during the course of the year that live up to the same promise. At the same time, the adidas brand increased its resources and focal point on apparel innovation with a clear focus on fit, feel and aesthetic. This will include the further development of the recently launched Alphaskin franchise, a rejuvenation of the Clima platform, as well as more iterations within exciting growth platforms such as Primeknit in the years to come.

WOMEN'S: A NEW DIMENSION TO DRIVE GROWTH

Winning the female consumer is an imperative for the adidas brand and offers tremendous growth potential. Women are active in all sports and, to a large extent, dominate social media and household shopping behavior. Given the magnitude of the business opportunity, in 2017, the adidas brand further invested resources in building a cross-functional women's organization and support infrastructure to set direction for creative, ranging, merchandising and marketing and to steer cross-category planning.

The adidas brand will relentlessly focus on five products for her: the bra, the tee, the tank, the tights and the running shoe. These are the five products the brand will innovate against, with the aim to create the best the industry has ever known in these five items. In 2017, the first results of this approach proved successful, with strong double-digit growth for our women's business resulting in an increase in the share of total business for the women's segment. A key highlight in this context was the launch of two global marketing campaigns: 'Unleash Your Creativity' telling the story of 15 female athletes who defy convention as well as a running-specific campaign 'Fearless AF', which aims to break down the stereotypes about female runners. In addition, the adidas brand increased its roster of female influencers around Karlie Kloss, Hannah Bronfman and Robin Arzon and continued to build on the partnership with Wanderlust, organizer of some of the largest yoga lifestyle events in the world.

MARKETING INVESTMENTS: MEAN MORE BY DOING LESS

The adidas brand is focused on creating inspirational and innovative marketing concepts that drive consumer advocacy and build brand equity. As a result, we are committed to continue increasing our absolute marketing investments going forward. While the brand currently spends almost half of its marketing investments on partnership assets, with the remainder on brand marketing activities such as digital, advertising, point-of-sale and grassroots activations, we will decrease the ratio of marketing investments spent on *promotion partnerships* [SEE GLOSSARY](#) to less than 45% by 2020. In addition, the brand will consolidate and focus resources to have the biggest effect on the creator and the brand's key franchises. This will be achieved by focusing on three priorities:

- **Reason to believe:** By harnessing the brand's creator positioning, the emotion of sport, and the power of sport to change lives, the adidas brand will communicate a reason to believe in the brand, letting the world know what distinguishes adidas from the competition.

- **Reason to buy:** The second priority is to harmonize and deliver globally consistent and impactful communication around the brand's key franchises. By investing more money against fewer items, the adidas brand will strive to elevate and maintain the iconic status of its key franchises, giving the consumer clear and compelling reasons to buy the product.
- **Sports communities:** Sports communities is where loyalty is built and earned. The adidas brand defines sports communities as those places where athletes are fully immersed in their sport with peers and friends. It's the football cage, the run base or the street court. Until 2020, the brand will therefore significantly step up its grassroots and local activation efforts, led by initiatives in the world's most influential cities.

In terms of partnership assets, while reducing the ratio of marketing spend and the number of partnerships, the adidas brand will nonetheless continue to bring its products to the biggest stages in the world through:

- **Events with global reach:** such as the FIFA World Cup, the UEFA EURO, the UEFA Champions League, Roland Garros (French Open) and the Boston Marathon.
- **High-profile teams:** such as the national association football teams of Germany, Spain, Argentina, Mexico, Colombia, Belgium and Japan, as well as top clubs such as Manchester United, Real Madrid, Bayern Munich, Juventus and Flamengo Rio de Janeiro in football, the New Zealand All Blacks in rugby, and American universities such as Miami, Arizona State and Texas A&M.
- **High-profile individuals:** such as football stars Lionel Messi, Paul Pogba, Gareth Bale, Mesut Özil and Gabriel Jesus, basketball stars James Harden, Damian Lillard and Andrew Wiggins, marathon record holder Dennis Kimetto, American football players Aaron Rodgers and Von Miller, baseball athletes Kris Bryant and Carlos Correa as well as tennis stars Garbiñe Muguruza and Alexander Zverev.

In addition, the adidas brand also has a number of strategic partnerships and creative collaborations in place. The strategic partnership with Kanye West is likely to be the most significant one ever created between an athletic brand and a non-athlete, while the collaboration between adidas Originals and Pharrell Williams remains highly influential. Top designers and design studios the brand works with include Yohji Yamamoto, Stella McCartney, Raf Simons, Gosha Rubchinskiy and Alexander Wang.

SUSTAINABILITY

The adidas brand is committed to sustainability and our strategic partnership with *Parley for the Oceans* [SEE GLOSSARY](#) serves as a prime example. adidas has changed the game by starting mass production of shoes using *Parley Ocean Plastic* [SEE GLOSSARY](#), and the brand continues to push for a more eco-innovative future. In 2017, we created more than one million pairs of shoes using Parley Ocean Plastic and restated our ambition to reduce the use of virgin plastic. During 2017, the initiative was extended to adidas Originals, yielding pioneering outcomes such as the EQT Support ADV Parley, as well as to apparel performance products in the form of four Major League Soccer (MLS) football jerseys.

[SEE SUSTAINABILITY, P. 88](#)

ROLE OF CATEGORIES

The adidas brand has assigned each category a role and ambition until 2020, allowing the brand to exploit short- and medium-term potential, while at the same time incubating long-term opportunities for the brand. There are four overarching roles: Lead, Grow, Amplify and Authenticate.

Lead

- To lead in the sporting goods industry, we believe it is a must to lead in the world's most popular sport, football. As such, the adidas brand aspires to be the number one football brand in every market by 2020. This will be driven

by focusing on winning the football creator in key cities as well as increasing investment in the brand's football footwear franchises. In 2017, the adidas brand pursued its full reset of its football footwear business with the continued focus on the 'X', Nemeziz and Copa franchises as well as playing off its strong product heritage with the re-introduction of the Predator.

- The adidas brand also strives for leadership in lifestyle in every market with Originals. Not only is adidas the original sports brand, it also was the first brand to bring sport to the street. Brand credibility and heritage is an important prerequisite to win the discerning streetwear hound consumer. These consumers are looking for substance and craft and are inspired by stories and design. Growth in this category will be driven by iconic products from the brand's past such as the Samba, Stan Smith, Gazelle and Superstar as well as pioneering new contemporary silhouettes inspired by elements from the past and the future, such as NMD, EQT, Tubular and Swift Runner, which account for approximately 50% of the adidas Originals footwear offering.

Grow

- The running category is the adidas brand's biggest growth opportunity across all genders and *price points* [SEE GLOSSARY](#). The brand's goal is to double sales in the category by 2020 compared to the 2015 financial year. Many innovations in the sports industry start in running. With groundbreaking innovation in materials such as Boost and pioneering new manufacturing processes being driven through Speedfactory, the timing is perfect for the adidas brand to strike in this category. To spur growth, amongst other things, adidas Running will significantly refine and evolve its franchise strategy for the male and female athlete, increase its investment in running communities and grassroots activations such as the Berlin and Boston

Runbases, as well as play a central role in driving the future of digital in sport in cooperation with Runtastic.

- The second category where the adidas brand is focused on driving significant market share gains is adidas Core. adidas Core targets a more price-conscious consumer, particularly in emerging markets, offering entry-price point styles across all categories. To ensure success, the adidas Core formula employs a 'fast fashion' business model. This means quick reaction to emerging trends through shorter lead times and excellence in retail execution.

[SEE INNOVATION, P. 78](#)

Amplify

- The training category is the adidas brand's largest performance category and is also the apparel engine of the brand. Led by cutting-edge innovation in fabrics and materials, the adidas brand aims to significantly increase its apparel footprint through Training, which provides products for general training purposes as well as for specific sports, as well as through Athletics, which is geared to capturing the sports mindset of every athlete off the pitch. Given the high visibility of its products in all markets, this category plays a central role in amplifying the brand message and DNA.

Authenticate

- In order to be the best sports brand in the world, the adidas brand also needs to be true to sports on a local level. As such, the brand will continue to cater to a wide range of sports such as golf, basketball, American football, baseball, outdoor, rugby, tennis, handball, volleyball, swimming and boxing. To maximize impact and resources, in key markets and cities, the adidas brand will prioritize those sports that are most significant in terms of local culture, participation and national pride.

REEBOK BRAND STRATEGY

MISSION: TO BE THE BEST FITNESS BRAND IN THE WORLD

Reebok is an American-inspired global brand with a deep fitness heritage and the mission of being the best fitness brand in the world. To realize this mission, the past years have been characterized by a transformation from traditional sports to fitness. The three sides of the Reebok Delta, a symbol of change and transformation, represent the physical, mental and social changes that occur when individuals embrace the challenge of bettering themselves in the gym, in their lives and in the world.

Throughout this journey, Reebok has invested in its training and running businesses to develop products that cater to all fitness routines, while returning to its fitness roots in Classics to support a fashion-forward lifestyle outside of the gym. Driven by its ambition to be the innovation leader in fitness, Reebok continues to merge its iconic past with new technologies that revolutionize both performance and lifestyle products.

CONSUMER OBSESSION: THE GAME CHANGERS

Reebok's consumer obsession focuses on being distinctive, relevant, and authentic with its focus consumers – the Game Changers. These consumers, equally women and men, of all ages, are driven by becoming their absolute best mentally, socially and physically. The Game Changers participate in a range of activities, are fitness-centric and are inspired by the broader fitness world. They share four essential qualities to create a unified mindset: self-betterment, perseverance, confidence and non-complacency. These are the core values that hold the Game Changers together. They blend fitness into their lives, care about style, and are passionate about what they do. Through robust research and interaction with consumers, Reebok has taken significant time to understand the complexities of their fitness lifestyle across both product

performance needs and style desires, and seeks to exceed expectations across the spectrum.

Within that consumer group, Reebok will continue to focus on the female Game Changers going forward. Rooted in Reebok's heritage, the brand is putting women at the heart of everything the brand does. This female-centric approach, with women being the focal point of content strategy, marketing activation and distribution, is a fundamentally different approach compared to other brands in the industry. It will allow Reebok to become truly dual-gender with the goal of its women's business representing 50% of the brand's net sales. In recent years, the brand has made significant strides in having a distinct position with women by signing prominent influencers that are relevant to her.

PRODUCT FRANCHISES: LEVERAGING THE BRAND'S FITNESS DNA

Reebok recognizes the importance of building strong footwear and apparel franchises, establishing innovative but repeatable product lines that become annuities for the brand and core items for the consumer. This is not only essential for enhancing consumer perception and brand consideration, but also essential for the efficiency of the Reebok brand.

For this reason, Reebok is heavily investing into franchises, making them a key priority going forward. By 2020, Reebok expects footwear franchises to represent at least 25% of the brand's total footwear business. Key franchises include *performance products* [SEE GLOSSARY](#) such as the CrossFit Nano or the recently launched FloatRide Run that have been authenticated by their respective communities, as well as styles that are unique to Reebok's fitness DNA, such as the Classic Leather and the Freestyle. In apparel, Reebok has established franchises specifically for women, such as the Lux Tight, which debuted in 2017. 2018 will see the introduction of

further apparel franchises focused on the female Game Changers.

Reebok puts a strong emphasis on innovation. The brand is committed to maintaining a full and innovative product pipeline, bringing new technologies, styles and processes to life. In this context, 2018 will see the launch of the PureMove Bra, a revolutionary sports bra featuring patented fabric technology that adapts to movement and intensity. Beyond technology platforms, Reebok is further investing into innovation that consumers can relate to, fostered by unique collaborations and stories. For example, in 2017 the brand launched the Reebok Innovation Collective, a consumer-facing platform to highlight this type of storytelling. [SEE INNOVATION, P. 78](#)

MARKETING INVESTMENTS: AMPLIFYING BRAND PURPOSE AND DRIVING SCALE

Reebok is focused on creating inspirational marketing capabilities that build brand equity and consumer advocacy, while unleashing powerful brand messages. A key element of Reebok's marketing and communication strategy is to connect emotionally to consumers through its 'Be More Human' platform, supported by a number of relevant assets and influencers in the digital ecosystem.

— **Be More Human:** Inspiring people to be their absolute best physically, mentally and socially is not only the brand's guiding principle, but also the essence of Reebok's global marketing campaign Be More Human. Launched in 2015, Be More Human celebrates everyday people who choose to embrace fitness and lead more fulfilling and less self-focused lives. A suite of films launched in 2017 marks the evolution of Be More Human, opening the aperture to even more types of fitness and people, but with the same message that physicality unlocks a better version of yourself. To celebrate the launch, ReebokONE trainers

were available across several US cities, offering workouts in exchange for a simple handshake as a way to physically and socially connect people through fitness. The campaign is supported by 'Stories of Progress', an online collection of inspirational influencer testimonials, and related content at brand events, retailers and Reebok FitHub locations.

- **Authentic and influential fitness assets:** To amplify the brand and increase its relevance vis-à-vis the fitness consumer, Reebok has entered into a series of partnerships with some of the world's most influential artists and athletes, such as Future, Gigi Hadid and J.J. Watt. In 2017, music artist Ariana Grande, actress Nina Dobrev and high-profile designer Victoria Beckham joined Reebok's strong roster of brand ambassadors. In addition, to validate its authenticity as the best fitness brand in the world, Reebok has entered into partnerships with some of the fastest-growing and most innovative organizations in the fitness world, such as CrossFit, Ragnar, Midnight Runners and Les Mills. Finally, continuing to build relationships with fitness instructors is a crucial component of Reebok's goal of connecting with the global fitness community. With over 100,000 fitness instructors currently being part of its global network, Reebok has made major progress towards its goal to be the brand of choice for instructors around the world.
- **Digital ecosystem:** Reebok is changing the way it operates digitally to realize maximum growth potential. The brand recognizes the need to be relevant and authentic in the digital ecosystem, particularly for women. As a result, this ecosystem is the main channel for communication and marketing initiatives as well as from a commercial perspective, providing experiences and products online. Reebok is focused on improving speed, usability and consumer experience on Reebok.com, both mobile and desktop, with 2018 seeing further enhancements to Reebok's digital ecosystem.

ROLE OF THE CATEGORIES

Running, Training and Classics each play vital roles for the Game Changers. Consequently, Reebok is focusing on those three categories to amplify its impact on the fitness enthusiast and leverage commercial opportunities from major fitness activities to lifestyle. Reebok Running's insight-driven and consumer-led approach supports authentic and desired cushioning experiences, leveraging innovative technologies for high-performance runners. Additionally, Reebok Running has also developed several contemporary silhouettes, which epitomize the intersection of innovation and style. Reebok Training remains central to Reebok's Game Changer mindset and offers a complete range of both highly specialized and versatile products that are at the forefront of fitness and true to the culture and community that Game Changers train and live in. Reebok Classics fuses the brand's fitness heritage with the modern looks of fitness reflected in Running and Training to support the Game Changer consumer who seeks to reflect a fitness lifestyle in every aspect of life.

'MUSCLE UP': REEBOK TRANSFORMATION STRENGTHENS BRAND FUNDAMENTALS

Over the last years, Reebok has made major progress in its transformation from a general sports brand to a 100% fitness-focused brand. While Reebok has recorded top-line growth for several years in a row, the brand's overall market share remains below levels seen in the past. In addition, there has been no growth in Reebok's home market, North America, in the recent past and the brand's margins are not accretive to the company's overall profitability.

Therefore, and as announced in 2016, Reebok continued to execute upon its turnaround plan 'Muscle Up' in 2017, aimed at accelerating Reebok's top-line growth in the US and improving its overall profitability. As part of this plan, the company has created one united team for Reebok in North America. As a result, Reebok's global and US organizations

were merged under one leadership team to streamline Reebok's organization and create an environment that is fully dedicated to fitness. In this context, Reebok moved its headquarters to a new location in the heart of the city of Boston during the course of 2017.

Furthermore, to win in North America, efficient and effective distribution is key to Reebok's future success in this all-important market. The company has therefore accelerated its initiatives to streamline Reebok's store base in the market. In total, the company will close nearly 50% of its own stores in the US market – both concept stores and factory outlets – with the majority of closures having been executed during 2017. At the same time, the brand is also streamlining its wholesale business, putting a clear focus on retailers helping Reebok to elevate brand equity and improve the quality of its growth.

In addition to streamlining Reebok's organizational set-up and progressing on the brand's turnaround efforts in the US market, an integral part of Muscle Up is focused on rethinking the core fundamentals of Reebok's end-to-end operations. Initiatives span across product development, go-to-market initiatives and marketing effectiveness to measures that help accelerate Reebok's product margins.

Executing against those initiatives will have a positive impact on Reebok's operational and financial performance and will accelerate the brand's top-line growth as well as significantly lift the brand's profitability in the years to come. In 2017, the first full year of executing Muscle Up, Reebok has already realized meaningful profitability improvements, as reflected by the brand's increase in gross margin of 4.0 percentage points to a level of 40.7%.

SALES AND DISTRIBUTION STRATEGY

TRANSFORMING THE MARKETPLACE

Our Global Sales function drives the commercial performance of the company by converting brand desire into profitable and sustainable business growth. It is our ambition to deliver the best shopping experience within the sporting goods industry across all consumer touchpoints. We strive to transform the marketplace by moving from managing the marketplace as it exists today toward shaping and growing our future destiny. Our objective is to establish scalable business solutions in order to deliver premium experiences, thereby meeting and surpassing consumer expectations with an integrated brand offering.

DRIVING OPERATIONAL EXCELLENCE ACROSS OUR GLOBAL MARKETS

Our sales strategy is crafted by a centralized and integrated marketplace team which supports the flawless execution of our brand strategies and drives operational excellence across the globe. In this context, in 2017 we continued to execute our strategic business plan until 2020, 'Creating the New', across our nine global markets. During the course of 2017, we also completed all preparatory work to consolidate the markets Greater China, Japan, South Korea and South-East Asia/Pacific, creating one consolidated market for Asia Pacific (APAC). This will allow us to better serve the converging consumer and customer demands in the region in the years to come. In a changing global landscape, our diverse market portfolio is an important asset in maximizing the business, elevating our competitiveness and achieving our ambitions towards 2020.

SEAMLESS CONSUMER JOURNEY ACROSS OUR CHANNELS

With more than 2,500 own-retail stores, around 13,000 mono-branded franchise stores and approximately 150,000

wholesale doors, we have an unrivaled network of consumer touchpoints within our industry. In addition, through our own e-commerce channel, our single biggest store available to consumers in over 40 countries, we are leveraging a consistent global framework. We are also seeing considerable success in leveraging our strong cross-functional partnerships with key wholesale partners, which is critical for ensuring a consumer journey to the full extent. By seamlessly integrating the channels within our market portfolio, we are uniquely positioned to pursue and succeed in strategies that deliver premium consumer experiences and increase the productivity of our distribution footprint. As we replicate this model to capitalize on new consumer opportunities through own retail destinations (own retail stores and own e-commerce sites) as well as our wholesale partner doors (wholesale managed spaces and e-wholesale) we create halo effects across all consumer touchpoints, resulting in further marketplace expansion.

In 2017, we advanced our sales strategy with several initiatives focused, amongst others, on premium consumer experience, marketplace transformation and productivity of the sales platform.

Premium consumer experiences

We aim to be 'omni-present' along the consumer journey and strive to capture the full sales potential on the platforms available to our consumers. We also strive to minimize occasions when consumer demand is not met, by offering innovative solutions. Based on these objectives, we focus on the following omni-channel initiatives:

- 'Inventory Check' which allows online shoppers to view in-store product availability.
- 'Click & Collect' which allows consumers to order online and purchase or reserve items for pick-up in a local store.

- 'Ship from Store' which allows us to service consumers faster than before by turning our stores into mini distribution centers.
- 'Buy Online, Return to Store' which not only provides consumers with a convenient way to return product purchases but also offers new buying opportunities.
- 'Partner Program' which enables us to expand our online offering to a larger group of consumers by making it available to selected key wholesale partners.
- 'Endless Aisle' which provides in-store visitors with access to our full range of products through our e-commerce platform.
- Our newly introduced 'adidas shopping App' is an always-on connection to the adidas brand and offers premium shopping experiences.

In 2017, we deployed a strategic mix of these capabilities across all our markets in our own-retail operations and at key wholesale partner locations. For example, based on the initial success of the Partner Program in 2016, we continued to onboard multiple partners across Western Europe and North America in 2017. In addition, 2017 saw the successful introduction of the adidas shopping App in Western Europe and the US. The App is directly linked to the adidas e-commerce store and provides consumers with personal conversations, a frictionless checkout, seamless order tracking as well as personalized content. The success of the App will be significantly enhanced by continued investments in Customer Relationship Management (CRM), which will enable us to develop a deeper consumer understanding and connection.

Marketplace transformation

Our goal is to leverage and scale the success of our initiatives across our channels to better serve consumers. The key contributor to this approach is controlled space. Whenever we can actively manage the way our brands and products are presented at the point of sale, the impact on the consumer

experience, and ultimately on our operational and financial performance, is significant. We have the power to do so in own retail (including e-commerce) and in wholesale (franchise stores, wholesale managed space and in e-wholesale). By 2020, we aim to generate more than 60% of our revenues through controlled space.

For us, own retail acts as a catalyst to our controlled space ambition. We amplify our success in own retail by translating key learnings to franchise stores and expanding franchising as a business model in existing as well as into new geographies. After the successful launch of our adidas flagship store in New York City in 2016, we opened our biggest ever adidas Originals flagship store in Chicago in 2017. We expect these flagships to set new standards in terms of product presentation, execution and service that will be replicated across all other channels. We expect e-commerce to continue to be the fastest-growing channel that we operate, with revenues forecast to grow to € 4 billion in 2020. In wholesale, we will continue to expand our footprint with a focus on prioritized key accounts, targeting important consumer hotspots and trade zones, especially those that are part of our Cities initiative. Strategic partnerships to operate controlled space remain an important thrust of this expansion.

Cities and trade zones

In 2017, we saw continued success in New York City, Los Angeles, Paris, London, Shanghai and Tokyo. The combined revenue growth for our six key cities outpaced the company's overall top-line development. In addition, our *Net Promoter Score (NPS)* [SEE GLOSSARY](#) relatively outperformed in most of these key cities. To further drive momentum, we will continue to prioritize consumer insights, retail executions and wholesale partnerships across those cities. We have also started to focus on those cities by looking at them on a trade zone level, rather than on a key account and key doors perspective. Our intention is to create one holistic premium

shopping experience for our consumers within these key commercial areas across all identified distribution points of wholesale and own retail. The learnings from this transformation program provide a further boost to our Cities strategic choice and enable us to scale this opportunity up, by rolling it out to a much greater number of cities where we will apply a focus of investments in areas where our focus consumers live, play and shop.

Specialty Sales

In 2017, we established the Specialty Sales organization. The objective of this organization is to drive brand heat and desire in boutiques and sneaker stores, thereby directly catering to our most influential consumers. The team provides superior service levels, customized range access across selected categories, such as running and Originals, as well as exceptional campaign roll-outs across the globe and has a clear alignment with our key cities and trade zones. Following initial success in 2017, with strong growth generated in boutiques and sneaker stores, we will continue to focus on growing our Specialty Sales initiatives in 2018 and beyond.

Productivity and efficiency of sales platform

We are committed to further driving productivity improvements across our sales platform through a multi-faceted approach:

- **Premium presentation:** Our physical selling spaces are an important factor in driving Net Promoter Score (NPS) and full-price sell-through. We further evolved the brand experience through the launch and expansion of premium store concepts such as *Stadium* [SEE GLOSSARY](#) and *Neighbourhood* [SEE GLOSSARY](#) for the adidas brand as well as *FitHub* [SEE GLOSSARY](#) for the Reebok brand. Our own-retail concepts are designed for scalability. Consequently, we will continue to roll them out across our store base, which yields benefits across channels, considering the positive spillover impact on our wholesale and franchise partners.

- **Consumer service excellence:** In 2017, we established the Sales Academy. The program helps us to transform the culture and effectiveness of our sales teams. As a result, consumers enjoy significantly elevated service levels which have proven commercially rewarding through higher *conversion rates* [SEE GLOSSARY](#) and increased average selling prices.
- **Personalized interaction:** Our commitment to deliver a premium shopping experience is reflected online through our digital brand flagship stores, adidas.com and reebok.com, as well as our newly created adidas shopping App. E-commerce and digital communication are powerful tools for our brands to engage with consumers.
- **Insight-driven decision-making:** We continue to invest in our analytical capabilities and technical infrastructure to become faster and more insight-driven in decision-making. Leveraging data such as cross-channel product sell-through and consumer purchasing behaviors delivers actionable insights in areas such as assortment planning and product life cycle management.
- **Distribution channel mix:** Based on a thorough analysis of the profitability of our distribution channels in each of our markets, in 2017 we started an optimization program to shift focus and resources to our most profitable channels. By doing so, we aim at further improving the distribution mix of our company and consequently the efficiency of our Global Sales organization.

We are confident that our sales strategy will help us realize significant improvements in brand desirability, as measured by our NPS, net sales, market share and profitability.

[SEE INTERNAL MANAGEMENT SYSTEM, P. 102](#)

GLOBAL OPERATIONS

Global Operations manages the development, production planning, sourcing and distribution of the vast majority of our products. The function strives to increase efficiency throughout the company's supply chain and ensures the highest standards in product quality, availability and delivery for our customers as well as our own-retail and e-commerce activities at competitive costs. ▽

CLEARLY DEFINED PRIORITIES FOR GLOBAL OPERATIONS

Global Operations delivers upon its mission to create the best product by focusing on innovative materials and manufacturing capabilities as well as to provide the best service by enabling product availability as the consumer chooses through the company's omni-channel approach to supply chain agility.

The strategy of Global Operations is an extension of the overall adidas strategy – thus the consumer is at the center of everything we do. The function strengthens brand desirability by providing the right product to consumers – in the right quality, size, color and style, in the right place, at the right time, across the entire range of the company's channels and brands. Additionally, Global Operations builds capabilities that further improve supply chain efficiencies, while mitigating costs, thereby ensuring a continuously competitive supply chain.

Within our strategic business plan 'Creating the New', Global Operations focuses on delivering against three strategic priorities driven by several initiatives:

- Become the first fast sports company.
- Create a seamless consumer experience.
- Transform the way we create and manufacture.

By delivering on these priorities, Global Operations leverages efficiencies across infrastructure and processes and ensures a competitive digital ecosystem and supply chain. This continues to be underlined by our 'On-Time In-Full' (OTIF) metric, a non-financial KPI for our company, measuring the adidas delivery performance toward our customers and our own-retail stores. ▽ SEE INTERNAL MANAGEMENT SYSTEM, P. 102 In 2017, adidas delivered 78% of its adidas and Reebok brand products 'on time' and 'in full' (2016: 77%), which is broadly in line with the overall target of around 80%. For 2018, Global Operations strives to increase OTIF further towards the targeted 80% level. OTIF was measured for 74% of net sales of all adidas and Reebok brand products in 2017. It is also planned to further roll out OTIF to those markets that are currently not in scope, thereby increasing the overall share of adidas and Reebok brand products measured against 'on time' and 'in full'.

BECOME THE FIRST FAST SPORTS COMPANY

'Speed' is a strategic priority for the company. Our ambition is to be the first fast sports company in the sporting goods industry. ▽ SEE CORPORATE STRATEGY, P. 62 Global Operations is a key enabler for this by leveraging market and sell-through data in new ways as well as by responding quickly to deliver concepts that are fresh and desirable and made available

when and where they are wanted by the consumer across our wholesale, retail and e-commerce channels. Bringing products to market faster allows our customers and direct-to-consumer channel to place orders closer to the actual time of sale, facilitating buying decisions that are based on better market knowledge. Consequently, we will move away from predominantly developing products in advance of seasonal merchandising calendars and toward creation and production capabilities that respond to consumer demands with in-season development and rapid replenishment manufacturing. Fresher and more desirable products will increase the company's full-price share of sales and reduce the risk of overbuying. In 2017, we made further progress around our Speed strategic priority and we are well on track to achieve our target of at least 50% of the company's net sales through speed-enabled articles by 2020. For this part of our business, we expect to achieve a 20% higher share of full-price sales compared to the regular range which, driven by higher brand and product desirability, will also see significant increases in the full-price sell-through.

In 2017, Global Operations continued to expand its efforts to 'enable later ordering' and further reduced production lead times. The function succeeded in providing 60 days or less production lead times on approximately 80% of apparel

Global Operations in go-to-market process

15



volumes throughout the year. The vast majority of footwear (around 85%) and hardware (around 95%) volumes are already on 60 days or less production lead times. In addition to shortening our overall production lead times, Global Operations has scaled its fast replenishment capabilities of best-selling articles, creating more articles within seasons based on actual sell-through data and ensuring constant availability of long lifecycle products. Across all product categories, replenishment capabilities have been established on 30 days production lead times. Even faster production lead times of on average less than 10 days have been established for customized footwear products, which are available via our own e-commerce website.

adidas is leveraging its strengths in sourcing and partnering with industrial and academic experts to develop smart manufacturing solutions that can react quickly to consumer trends. In this context, *Speedfactory* [SEE GLOSSARY](#) is one initiative, aimed at moving production closer to key markets while developing high-quality performance products faster than ever before. Powered by end-to-end automated manufacturing processes and innovative materials, Speedfactory allows us to support the growing demand for product personalization in a socially and environmentally responsible way. In addition, it helps us to provide faster reaction times to consumer needs and to enhance the consumer experience, by enabling consumers to co-create in an interactive production process. Insights gained from our Speedfactories will enable us to drive digital manufacturing also into our existing supply chain. [SEE CORPORATE STRATEGY, P. 62](#)

CREATE A SEAMLESS CONSUMER EXPERIENCE

Global Operations has a strong track record for establishing state-of-the-art infrastructure, processes and systems that are required to support the company's growth ambition. It has been successfully consolidating and improving legacy structures, thereby reducing complexity and costs for the

company. The function is focused on innovative distribution capabilities, with the goal of providing the best service by enabling product availability as the consumer chooses through the omni-channel approach to supply chain agility.

By creating a higher commonality of our products across the various channels, Global Operations ensures higher flexibility at each consumer touchpoint. This, in turn, enables a broader range of products to be available at the point of sale, including online orders able to be picked up in our own-retail stores or shipped from a store and own-retail stores able to sell inventory available in other own-retail stores. [SEE SALES AND DISTRIBUTION STRATEGY, P. 72](#)

In 2017, Global Operations focused on further optimizing its distribution center network, while at the same time preparing it for future consumer demand and supporting the company's overall growth ambition. In this context, in 2017 we continued to build two new distribution centers in Rieste/Germany and Suzhou/China - both of which are expected to go live in 2018. In addition, we started with the construction of a new distribution center in Pennsylvania/USA and began to expand our existing West Coast facility, aimed at supporting our future growth expectations for North America, in particular around the company's e-commerce and own-retail businesses. Lastly, to improve our consumer service in the UK, 2018 will see the addition of a new e-commerce facility to our existing distribution network in the market.

TRANSFORM THE WAY WE CREATE AND MANUFACTURE

Global Operations is driving innovation in new materials, new product constructions and new ways of manufacturing that deliver consumer value and enable competitive advantage. By investing in tools that more directly connect design and factory production, Global Operations is changing traditional models of development to deliver constant freshness and

increased speed-to-market capabilities. At the same time, the function also plays a critical role in driving operational efficiency for the company. In particular, through material and packaging consolidation, Global Operations aims at mitigating material and labor costs.

We constantly look for the next generation of materials by focusing, amongst others, on knitted footwear, direct-to-textile digital printing and sustainable materials. Building on our successful partnership with *Parley for the Oceans* [SEE GLOSSARY](#), 2017 saw the introduction of new footwear and apparel products using sustainable materials. In 2018, we will continue to roll out *Parley Ocean Plastic* [SEE GLOSSARY](#) across our key categories, with running footwear and football apparel playing a major role. To facilitate the growing demand for Parley Ocean Plastic we are in the process of establishing an operations set-up dedicated to sustainable material sourcing. [SEE SUSTAINABILITY, P. 88](#)

Through its focus on 'Digital Creation', Global Operations has already started to improve the product creation process from concept to shelf. Based on 3D software tools, we are today able to look at product solutions the way the consumer sees them at an early stage during the creation process. This enables creation teams to iterate faster, take product decisions quicker and reduce *drop rates* [SEE GLOSSARY](#). In addition, 3D technology allows for more frequent and rapid virtual product iterations without increasing the need for physical samples. After testing 3D software tools across all major business units in 2016, many of our business units have started to leverage 3D technology as a new way of working in the product creation process during 2017.

In addition to focusing on managing a more concentrated portfolio of key footwear franchises, Global Operations also continues to implement its modular approach to our apparel business. Transitioning to a set pre-season selection of

standard product features and driving consistent executions across categories for core products has been underway for several seasons in apparel. Meanwhile Global Operations has fully embedded the modular approach to creation, enabling us to ensure a consistent brand footprint, capture cost savings through factory efficiencies and reduce production lead times. In 2017, Global Operations further incorporated our new digital creation tools into the modular approach, which further increases speed in the creation process and allows us to leverage automation opportunities. Going forward, we will continue to gradually roll out our digitized capabilities and tools to progress on our vision of an end-to-end digital value chain from pre-season planning to product creation, production and sales. In this context, in 2018 we will set the foundation for the exciting endeavor of 'end-to-end Digital Creation' and will focus our efforts toward developing the new holistic digital creation framework.

Driving the level of automation in our supply chain remains of overriding importance for Global Operations. In this context, auto cutting and auto stitching are important focus areas, as they allow us to reduce our dependency on manual labor while at the same time ensuring consistent and highest quality standards. To further improve our production efficiency, we will accelerate the level of automation in our supply chain in the years to come.

MAJORITY OF PRODUCTION THROUGH INDEPENDENT SUPPLIERS

To keep our production costs competitive, we outsource almost 100% of production to independent third-party suppliers, primarily located in Asia. While we provide them with detailed specifications for production and delivery, these suppliers possess excellent expertise in cost-efficient, high-volume production of footwear, apparel and hardware. SEE GLOSSARY. Working closely with key strategic partners, the vast majority of our products are produced in 109 manufacturing

facilities worldwide. We value long-term relationships: Around half of our strategic suppliers have worked with adidas for more than ten years and, of these, close to 15% have a tenure of more than 20 years. SEE DIAGRAM 16 The length of our supplier relationship is determined by specific performance criteria which is regularly measured and reviewed by Global Operations. The latest list of our suppliers can be found on our website. ADIDAS-GROUP.COM/SUSTAINABILITY adidas also operates a limited number of own production and assembly sites in the USA (2), Canada (1) and Germany (1). In order to ensure the high quality that consumers expect from our products, we enforce strict control and inspection procedures at our suppliers and in our own factories. Effectiveness of product-related standards is constantly measured through quality and material claim procedures. In addition, we track social and environmental performance criteria of our suppliers through the C- and E-KPI tracking system. Adherence to social and environmental standards is promoted throughout our supply chain. SEE SUSTAINABILITY, P. 88

Strategic supplier relationships 16

	Total	Hardware	Apparel	Footwear
Number of strategic suppliers	109	15	60	34
Average years as strategic supplier	11.4	12	10	13
% of all production volume	83%	50%	85%	90%
Strategic relationships < 5 years	16%	27%	15%	12%
Strategic relationships < 10 years	37%	20%	45%	29%
Strategic relationships < 15 years	20%	20%	17%	26%
Strategic relationships < 20 years	13%	0%	17%	12%
Strategic relationships < 25 years	8%	20%	3%	12%
Strategic relationships > 25 years	6%	13%	3%	9%

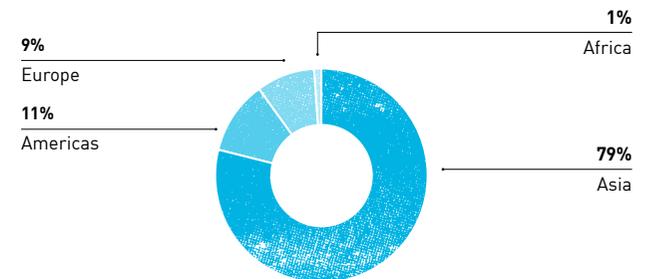
WORKING WITH 296 INDEPENDENT MANUFACTURING PARTNERS

In 2017, Global Operations worked with 296 independent manufacturing partners (2016: 297). Of our independent manufacturing partners, 79% were located in Asia (2016: 80%), 11% in the Americas (2016: 12%), 9% in Europe (2016: 7%) and 1% in Africa (2016: 1%). SEE DIAGRAM 17

VIETNAM SHARE OF FOOTWEAR PRODUCTION INCREASES SLIGHTLY

97% of our total 2017 footwear volume was produced in Asia (2016: 97%). Production in Europe and the Americas combined accounted for 3% of the sourcing volume (2016: 3%). SEE DIAGRAM 18 Vietnam represents our largest sourcing country with 44% of the total volume (2016: 42%), followed by Indonesia with 25% (2016: 24%) and China with 19% (2016: 22%). In 2017, our footwear suppliers produced approximately 403 million pairs of shoes (2016: 360 million pairs). SEE DIAGRAM 19 Our largest footwear factory produced approximately 11% of the footwear sourcing volume (2016: 10%).

Suppliers by region¹ 17



¹ Figures include the adidas and Reebok brands, adidas Golf and Ashworth, but exclude local sourcing partners, sourcing agents, subcontractors, second-tier suppliers and licensee factories.

CHINA REMAINS LARGEST SOURCE COUNTRY FOR APPAREL

In 2017, we sourced 93% of the total apparel volume from Asia (2016: 93%). The Americas represented 4% of the volume, Europe 3% and Africa 1% (2016: the Americas 3%, Europe 4% and Africa less than 1%). [SEE DIAGRAM 20](#) China is the largest source country, representing 23% of the produced volume (2016: 27%), followed by Cambodia with 22% (2016: 22%) and Vietnam with 18% (2016: 17%). In total, our suppliers produced approximately 404 million units of apparel in 2017 (2016:

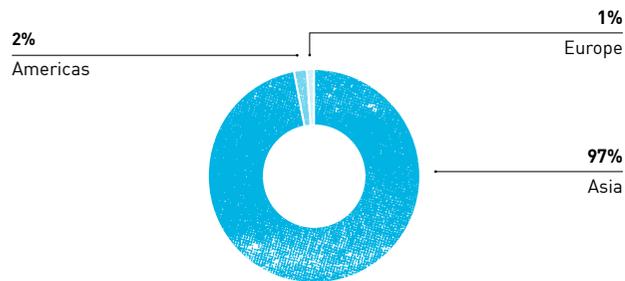
382 million units). [SEE DIAGRAM 21](#) The largest apparel factory produced approximately 10% of this apparel volume in 2017 (2016: 11%).

CHINA SHARE OF HARDWARE PRODUCTION INCREASES

In 2017, 82% of our hardware products, such as balls and bags, was produced in Asia (2016: 79%). European countries accounted for 16% (2016: 18%), while the Americas represented 2% of the total volume (2016: 3%). [SEE DIAGRAM 22](#)

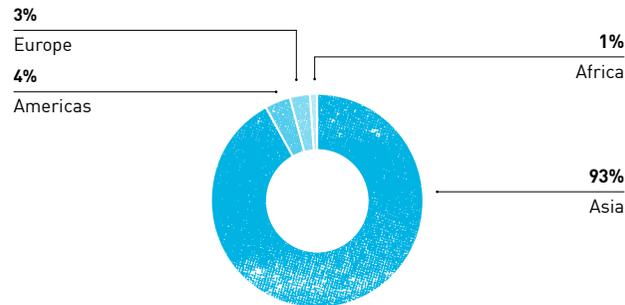
China remained our largest source country, accounting for 40% of the sourced volume (2016: 36%), followed by Pakistan and Turkey with 18% and 15%, respectively (2016: 17% and 16%, respectively). The total hardware sourcing volume was approximately 110 million units (2016: 109 million units), with the largest factory accounting for 15% of production (2016: 12%). [SEE DIAGRAM 23](#)

Footwear production by region¹ 18



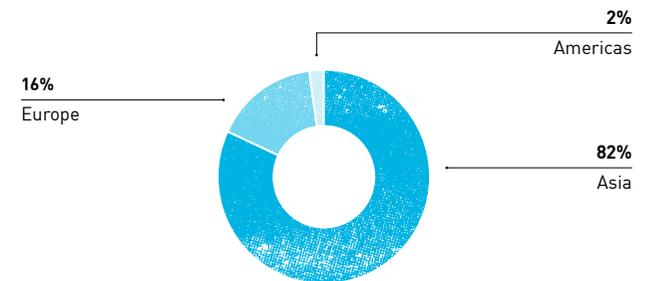
¹ Figures include the adidas and Reebok brands, adidas Golf and Ashworth.

Apparel production by region¹ 20



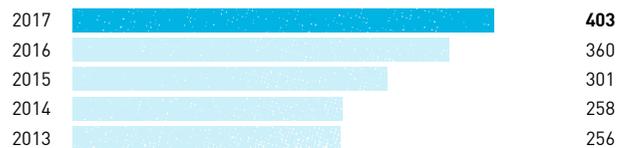
¹ Figures include the adidas and Reebok brands, adidas Golf and Ashworth.

Hardware production by region¹ 22



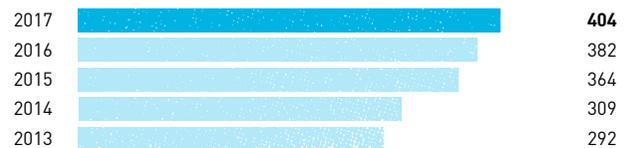
¹ Figures include the adidas and Reebok brands, adidas Golf and Ashworth.

Footwear production¹ in million pairs 19



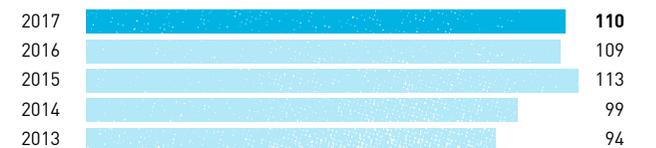
¹ Figures include the adidas and Reebok brands, adidas Golf and Ashworth.

Apparel production^{1,2} in million units 21



¹ Figures include the adidas and Reebok brands, adidas Golf and Ashworth.
² 2013 restated due to a reclassification of certain apparel accessories from apparel to hardware.

Hardware production^{1,2} in million units 23



¹ Figures include the adidas and Reebok brands, adidas Golf and Ashworth.
² 2013 restated due to a reclassification of certain apparel accessories from apparel to hardware.

INNOVATION

Creating innovative products to meet the needs of professional and everyday athletes as well as consumers is a prerequisite to strengthening our market position in the sporting goods industry and a premise to being the best sports company in the world. We therefore remain highly committed to maintaining a full and innovative product pipeline, bringing new groundbreaking technologies and processes to life, investing into forward-looking and sustainable ways of production and exploring the many possibilities of digitalization across our entire value chain. True to the vision of creative collaboration, our innovation approach is widely based on our Open Source mindset which is clearly visible in our numerous collaborations with athletes and consumers, universities, industry-leading companies as well as national and international governments and research organizations.

MEETING THE NEEDS AND EXPECTATIONS OF OUR CONSUMER

Innovation within the company follows a decentralized approach. In line with their respective strategic and long-term visions and distinctive positioning, each brand runs its own innovation activities. However, fundamental research as well as expertise and competencies in sustainable product creation are shared across the company.

For the adidas brand, innovation is focused on meeting the needs and expectations of our consumer. The modern innovation landscape extends beyond product and increasingly requires innovation teams to consider the development of experiences and services and to provide greater levels of transparency and direct integration of our consumer through co-creation. In partnership with our consumer insight teams, foresight and trend analysis efforts are shared on an ongoing basis, documenting shifts in society

and culture. This provides the starting point to build concepts of relevance.

The FUTURE team at adidas is tasked to develop a strong portfolio of innovation capabilities such as new materials, production processes and consumer-centric scientific research to provide a platform for meaningful concept development. Projects are incubated within the company and aligned to the broader sourcing, marketing, creative and strategic functions across the organization, ensuring a robust and impactful innovation pipeline.

To further strengthen long-term research capabilities, adidas implemented a centralized project team in 2017 in order to drive the process for the application and management of publicly funded research projects. Located within the FUTURE team, the team is responsible to collaborate with governmental organizations on local, national and European level to develop key projects with strong consortia partners, tackling major societal challenges that will impact our consumer and industry.

This approach also reflects our commitment to the Open Source mindset, where we seek to build value together with athletes and consumers, universities, industry-leading companies as well as national and international governments and research organizations. In addition to opening up our doors to valuable feedback, we also get inspired by and receive input from knowledgeable and valued partners. Whether we work with Parley for the Oceans on products partially created from upcycled plastic waste ('Parley Ocean Plastic' [SEE GLOSSARY](#)), intercepted before it reaches the ocean from beaches and coastal communities, with BASF, the world's leading chemical company, on Boost, an industry-first cushioning technology designed to deliver maximum energy return, responsiveness and comfort to athletes, or Speedfactory, a revolutionary automated production concept

in cooperation with Oechsler AG, Manz AG, BASF and Kurtz Ersä – we will continue to unlock further potential through collaborations. In addition to these already established partnerships, we announced a new collaboration with Siemens, a global leader in the fields of industry, energy and healthcare, as well as for infrastructure solutions, to drive the digitalization of Speedfactory. In addition, we commenced a partnership with Carbon, a Silicon Valley-based tech company working to revolutionize product creation through hardware, software and molecular science, to enable mass production of additively manufactured components, coming to life in the Futurecraft 4D, the first performance footwear crafted with light and oxygen.

FIVE PILLARS OF INNOVATION

Within our innovation principles, we identified five strategic pillars, which enable us to develop the best products and experiences for athletes and consumers, while at the same time drive game-changing innovations in the fields of manufacturing, digital and sustainability.

Athlete innovation

Our clear focus is to produce the best and most innovative products for athletes to enable them to perform at their very best. To achieve this, we work closely together with athletes and teams as well as numerous universities and industry-leading companies, to deliver against the needs of our target consumer.

Manufacturing innovation

To simplify manufacturing, enable product innovation and increase speed-to-market capabilities by bringing the production of apparel and footwear closer to the consumer, the company's innovation activities are also focused on new manufacturing technologies. Our goal is to combine state-of-the-art information technology with new manufacturing processes and innovative products. For this reason, we

commit ourselves to long-term cooperation with industry-leading companies and organizations to take a leading role in manufacturing innovation.

Digital and experience innovation

The adidas brand was amongst the first in the industry to comprehensively bring data analytics to the athlete. With decades of continuous investment in sports science, sensor technology and digital communication platforms, adidas has already taken a leading role in terms of changing the sporting goods industry through technology. With the increasing speed of digitalization, this field will remain one of our core areas.

Sustainability innovation

Our commitment to manage our business in a responsible way has long been one of the company's principles. To stay at the forefront of sustainable innovation, adidas is pursuing a proactive approach to establish internationally recognized best practices and achieve scalable improvements. As part of our sustainability roadmap we have set ourselves the target for 2020 to invest in materials, processes and innovative machinery which will allow us to upcycle materials into products and reduce waste. [SEE SUSTAINABILITY, P. 88](#)

Female athlete innovation

Our long-term commitment to the female athlete continues to be a focus for the company. To fuel the growth of our women's business, we have taken a holistic approach to understanding the female athlete's performance and non-performance needs throughout her active life by looking at this target group as an integrated part of our business but from a separate and unique angle. With a focus on the female athlete, it is crucial to fully understand the particular anatomy and specific product needs of the female consumer to help unlock her full potential. To enable this, we are working to establish a robust network of industry leaders and academic experts with our 'Path to Expert' approach, which will help to accelerate the

building of insights and foresights that keep us at the forefront of product innovation.

SUCCESSFUL COMMERCIALIZATION OF INNOVATIONS

We believe developing industry-leading technologies and user experiences is only one aspect of being an innovation leader. Equally important is the successful commercialization of those technological innovations:

Futurecraft 4D: High-performance footwear featuring midsoles crafted with light and oxygen using Digital Light Synthesis, a technology led by Carbon. The Futurecraft 4D's midsole pioneers a digital footwear component creation process that eliminates the necessity of traditional prototyping or molding. With the new technology, adidas now operates on a completely different manufacturing scale and sport performance quality, officially departing from 3D printing and bringing additive manufacturing in the sports industry into a new dimension. Ultimately, adidas aims to create more than 100,000 pairs of this high-performance footwear by the end of 2018.

adizero Sub2: A high-performance marathon shoe created to take athletes below the two-hour barrier. It explores the performance of a range of state-of-the-art materials in different temperatures and environments and on different surfaces. The shoe delivers the best of adidas running technology in an extremely fast, lightweight form and marks the debut of adidas' new Boost Light innovation. Engineered specifically for elite athletes on race day, Boost Light is the brand's lightest-ever foam and retains the industry-leading energy return.

UltraBOOST X: A lightweight running shoe for the female runner, featuring a Boost midsole, an adaptive arch as well as a Primeknit upper for perfect fit and flexibility. The ARAMIS system, a motion tracking technology that enables a detailed

analysis into the movement of the body, was used to allow adidas' innovation teams to see exact points where female runners need the most support and where their foot needs room for natural expansion. This process led to the unique design of the UltraBOOST X shoe.

AM4 Series: The first major project to be created at the adidas Speedfactory facility in Ansbach, Germany and in 2018 also in Atlanta, USA. The adidas Made For London (AM4LDN) and the adidas Made for Paris (AM4PAR) shoes are the first in a series of individually designed and manufactured running shoes adidas will release in six key cities around the world. In the coming months, Los Angeles, New York, Tokyo and Shanghai will also have bespoke product created tailored to the unique demands and using local market insight of each respective city.

Prime SP Parley: The first 3D knitted sprint spike, created with plastic taken from beaches and coastal communities before reaching the oceans. The silhouette focuses both on the needs of sprinters, by incorporating a Primeknit upper for support and a laser-welded frame for reduced weight, and on the needs of the world, by integrating Parley Ocean Plastic and protecting our oceans from marine plastic pollution.

adidas Alphaskin: A new base-layer technology constructed to match the body's movements in sport. Alphaskin was developed using the ARAMIS motion-capture system instead of a traditional static mannequin for testing, in order to find out where fabric constrains an athlete's performance. The new design eliminates seams to help athletes focus on their performance in competition and training. Alphaskin offers kinetic wrapping in a range of compression levels that suit each athlete's personal preference.

Reebok Floatride Run: The first shoe featuring Reebok's new Floatride Foam technology. The unique and consistent cell structure of Floatride Foam delivers soft, responsive

cushioning without compromising weight, so runners can ‘float’ through their run. The one-piece Ultraknit upper is engineered in zones to offer support and breathable flexibility. Seamless construction and a 3D heel cradle limit irritation while locking in a comfortable fit.

Reebok Cotton + Corn: The initiative is intended to bring plant-based footwear to the market in 2018. The first shoe ‘made from things that grow’ will have an upper comprised of organic cotton and a base originating from industrial grown corn, which is a non-food source. For the Cotton + Corn initiative, Reebok partnered with DuPont Tate & Lyle Bio Products, a leading manufacturer of high-performance bio-based solutions.

The awards the company has attained for its innovations confirm our continuous efforts to become the innovation leader in the sporting goods industry. In 2017, for example, the Futurecraft 4D was awarded with the ‘Fast Company’s Innovation by Design Award 2017’ and named one of the 25 best innovations 2017 by Time Magazine. Also, we were named ‘Game Changer 2017’ in the category ‘Operations of the Future’ by Manager Magazin and Bain & Company for executing innovative solutions such as Futurecraft 4D, Speedfactory and Parley. In addition, the Reebok Floatride Run was named ‘Best Debut’ in the 2017 Runner’s World Summer Shoe Guide.

NEW PRODUCT LAUNCHES GENERATE THE MAJORITY OF SALES

As in prior years, the majority of sales were generated with products newly introduced in the course of 2017. New products tend to have a higher gross margin compared to products which have been in the market for more than one season. As a result, newly launched products contributed overproportionately to net income in 2017. We expect this development to continue in 2018 as we will present a wide range of new, innovative products. [SEE SUBSEQUENT EVENTS AND OUTLOOK, P. 128](#)

In 2017, brand adidas and Reebok sales were again driven by the latest product offerings. At brand adidas, products launched during the course of the year accounted for 79% of brand sales (2016: 77%), while only 2% of sales were generated with products introduced three or more years ago (2016: 1%). At Reebok, 69% of footwear sales were generated by products launched in 2017 (2016: 73%). Only 12% of footwear product sales relate to products introduced three or more years ago (2016: 11%).

R&D EXPENSES INCREASE 25%

Expenses for research and development (R&D) include expenses for personnel and administration, but exclude other costs, for example those associated with the design aspect of the product creation process. In 2017, as in prior years, all R&D costs were expensed as incurred. The company’s R&D expenses increased 25% to € 187 million from € 149 million in the prior year.

As our R&D departments comprise experienced and multi-skilled people from different areas of technical expertise and from diverse cultural backgrounds, personnel expenses represent the largest portion of R&D expenses, accounting for 64% of total R&D expenditure.

The number of people employed in R&D activities at December 31, 2017, was 1,062, compared to 1,021 employees in the prior year. This represents 2% of total employees.

In 2017, R&D expenses represented 2.1% of other operating expenses (2016: 1.9%). R&D expenses as a percentage of sales increased to 0.9% (2016: 0.8%). [SEE TABLE 24](#)

Key R&D metrics ^{1,2}

24

	2017	2016	2015	2014	2013
R&D expenses (€ in millions)	187	149	139	126	124
R&D expenses (in % of net sales)	0.9	0.8	0.8	0.9	0.9
R&D expenses (in % of other operating expenses)	2.1	1.9	1.9	2.0	2.0
R&D employees	1,062	1,021	993	985	992

¹ 2017 and 2016 figures reflect continuing operations as a result of the divestiture of the Rockport, TaylorMade, Adams Golf, Ashworth and CCM Hockey businesses.
² 2015, 2014 and 2013 figures reflect continuing operations as a result of the divestiture of the Rockport business.

PEOPLE AND CULTURE

At adidas, we believe that our people are the key to the company’s success. Their performance, well-being and knowledge have a significant impact on brand desire, consumer satisfaction and, ultimately, our financial performance. Through the delivery of our People Strategy, we focus our efforts on four fundamentals: the attraction and retention of the right talents, role model leadership, diversity and inclusion, as well as the creation of a unique corporate culture.

PEOPLE STRATEGY ENABLES A CULTURE FOR DELIVERING ‘CREATING THE NEW’

As an integral part of our corporate strategy ‘Creating the New’, the People Strategy is a testament to thinking that our 2020 strategy can only be executed if we speak to our people

on all levels and win both their hearts and minds. The People Strategy consists of four pillars that serve as a basis for creating the culture and environment for our people in order to successfully support Creating the New. [SEE DIAGRAM 25](#) These four pillars also serve as a tool for prioritization, sense-checking and measuring our HR actions and initiatives. The People Strategy is implemented through a portfolio of projects which will directly deliver into each of the four pillars. In 2017, we made good progress by delivering the following initiatives.

Meaningful reasons to join and stay

Kicked off in 2015, our internal career development program Talent Carousel entered its third year, with the first generation graduating in 2017. The program encourages employees from all over the world to apply and become one of 20 finalists to take a cross-functional and international career step by starting a new role in a new location. Candidates remain in the

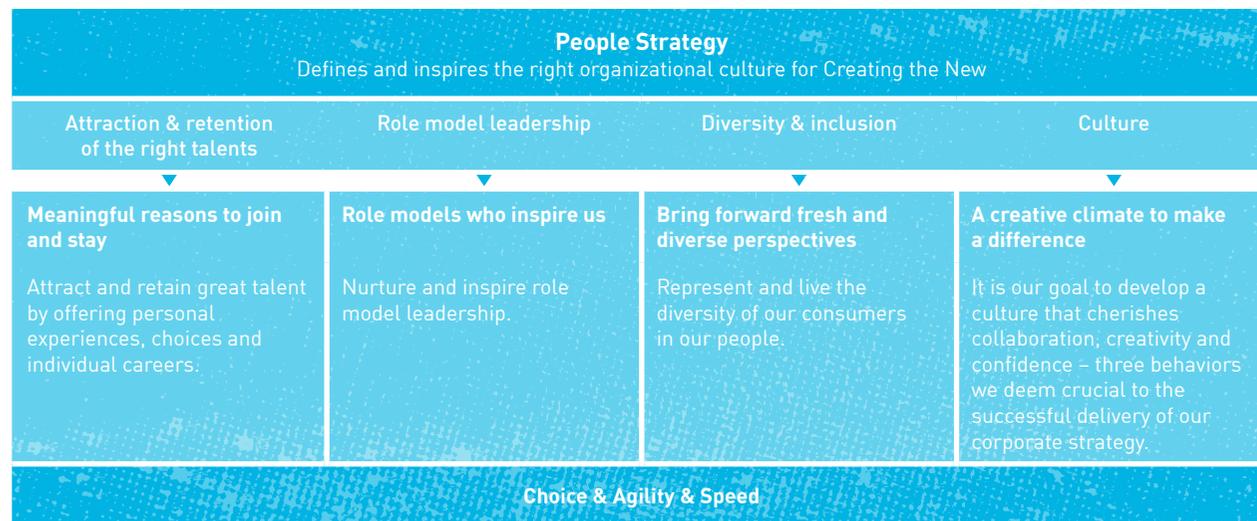
program for 24 months with the right to return to their home location while being developed with the goal of them assuming Senior Management positions in the future.

In 2017, we continued our central onboarding process at our headquarters in Herzogenaurach, Germany, which ensures new starters enjoy a high-quality, consistent experience upon joining the company. In addition, we piloted a digital pre-onboarding app available initially to new joiners in our Digital Brand Commerce teams across Herzogenaurach, Portland, Amsterdam and Zaragoza. The app allows us to engage with new hires immediately upon their signing of an employment contract. Through research into other organizations, we learned that connecting with new joiners and providing them with a cultural onboarding before their first day on the job shortens their ramp-up time as it reduces complexity in the initial stages, ensuring they are highly engaged from day one. Both our pre-onboarding platform and in-person experience provide important learnings for a global onboarding initiative which aims at introducing standard onboarding tools in the next two years.

Our Learning Campus provides access to learning opportunities for employees globally. Through this digital platform, our people are able to develop skills to support their current performance and future career development. In 2017, we saw additional functional learning opportunities become accessible under the Learning Campus umbrella.

Introduced in 2016 in Germany, the US, the Netherlands and Hong Kong, our employee Stock Purchase Plan was rolled out to Greater China, Taiwan and the Hong Kong market organization in 2017. By the end of the year, 45% of our total employee population were eligible to take part in the program, and around 3,600 decided to participate. It is planned to extend this program to further countries in the coming years.

The four pillars of our People Strategy



Our offices in the Netherlands, Spain and China received awards from the Top Employer Institute for their efforts to provide an exceptional work environment for our people. With its certification, the Top Employer Institute recognized adidas' People Strategy, its organization-wide Learning & Development framework which encourages different kinds of learning and its career management model. adidas promotes and encourages employee mobility across the organization and holds line managers accountable for developing the succession pipeline.

In the neighboring forest at our headquarters, we opened the company's first-ever outdoor kindergarten group with 20 children, extending our child-care offer in a unique way. Also, we laid the foundation stone for our second day-care center on campus. It will open in October 2018, providing spots for a total of another 138 children: 75 for kindergarten children, 48 for nursery children, and 15 spots for short-term or emergency day care.

Role models who inspire us

In 2017, we made significant progress with this People Strategy pillar. Two new leadership groups were created, with a third one in the making:

- The Core Leadership Group (CLG) is the most senior group, made up of around 20 members from our Executive Leadership population. Members of this group jointly represent top positions and roles across our company. These functional and geographical experts partner with the Executive Board in teaching and overseeing the cross-functional execution of the Creating the New strategy, accelerating its delivery, as well as mentoring and sponsoring the next generation of leaders. The CLG also serves as the succession pool for the Board.
- The Extended Leadership Group (ELG) currently has around 100 members. This new community of leaders collaborates across functions to lead the implementation

of the strategic initiatives that form the Creating the New portfolio as well as the functional and market project portfolios. They drive continuous improvement across the organization and also mentor and sponsor younger leaders. The ELG serves as a succession pool for the CLG.

- A third group – the Global High Potential Group (GHIPO) – will be formed in the first quarter of 2018. Within this group, which will consist of 50 members, we are striving for a 50:50 gender balance. With the GHIPO group we want to identify and develop high potentials who have the ability to take on more complex, demanding and higher-level responsibilities at a global executive level. The GHIPO program will develop participants' capability against a consistent future Senior Management profile.

In an effort to drive clarity and accountability, the CLG has created the company's first global Leadership Framework. It is based on the three company behaviors creativity, collaboration, confidence (the '3Cs') and articulates the particular behaviors that are expected of leaders at adidas. The framework was developed jointly with employees worldwide who provided feedback on what great leadership within adidas looks like to them. It now provides a global and universal language that is inclusive, reduces the need for local interpretations and outlines concrete behaviors that serve as a measure of leadership effectiveness. It will also be built into the way we hire and promote as well as rate performance. The framework was activated and cascaded to employees globally through the CLG and ELG groups. Employees' awareness of the framework as well as its overall effectiveness are measured via our monthly employee experience survey 'People Pulse'.

We continued to deliver our people manager training 'Fit2Lead' across the US, Asia and EMEA (Europe, Middle East and Africa). This training is specially designed for all first-time people managers who lead up to five people. It provides them

with basic knowledge on how to become a good people manager, manage their business and continue to develop themselves throughout their career. The course can also be booked by managers who would like to refresh their people management skills. Since 2016, this curriculum is complemented by the 'Fit2Lead Experienced Manager' training that is geared towards managers who bring more than five years of management experience and/or lead or influence larger teams.

Bring forward fresh and diverse perspectives

We delivered our 'BIG Deal' gender intelligence training to the Board and their direct reports, covering 387 executives across nearly all our market subsidiaries within the course of a year. 'BIG' stands for Balanced, Inclusive, Gender Intelligent. BIG Deal is a one-day workshop designed to give participants new insights and practical tools that support them in building an inclusive company culture. Participants are challenged to revisit and think critically about some of their key thoughts and beliefs around diversity, stereotyping and gender in the workplace.

Functional and local market teams continued to develop dedicated plans to invest in a stronger female talent pipeline, data analysis on gender balance and action plans to establish a more balanced organization in terms of gender, age and origin.

Our employee resource groups across the organization with an employee base of more than 700 members per group regularly hold awareness events and activations garnering corporate support for topics such as women's, LGBTQ, age and origin as well as giving employees from all walks of life a voice.

A creative climate to make a difference

In a continued effort to provide our employees with the best work environment possible, further construction work has started on our headquarters campus in Herzogenaurach. A

new building called 'Arena' will become the company's new main office in the first half of 2019, offering over 2,000 employees a new home, centralizing most of the employees in Herzogenaurach on the World of Sports campus. 2017 also saw the construction of a third future workplace space, 'Base', following the successes of 'Pitch 1' and 'Pitch 2'. Employees based in these buildings work according to the activity-based working concept. They no longer have assigned desks but can choose from a multitude of different types of rooms and spaces based on the tasks they have on hand. Change management in these new buildings is supported through a dedicated mobile app as well as employee-led feedback groups and regular feedback surveys.

Our 'MakerLabs' at our headquarters in Herzogenaurach and in Portland, USA, serve as dedicated spaces providing tools such as laser cutters and 3D printers and know-how to help employees realize their ideas and create prototypes. The 'MakerLab' idea has its roots in the 'hacker space' concept, where all employees are given free rein to create and bring their ideas to life. ▽

HR FOUNDATIONS FOR OUR PEOPLE STRATEGY

▣ In 2017, the adidas HR function further evolved People OneView – a self-service online portal that allows employees, leaders and HR Partners to both access and manage the most important personal and work data such as salary, career and team information as well as HR applications. By providing direct access to People OneView, users are empowered to manage their most important personal data without having to go via their HR Partner. HR Partners in turn regain valuable time to counsel and support employees. In 2017, two new modules were added to the platform: Dashboarding gives HR Partners and senior leaders access to certain HR-specific metrics and standard reports, Org Viewing provides all employees with full transparency over the organizational structure of the company.

The year was also focused on further stabilizing and enhancing the HR Shared Service Center function for Germany. All employee queries relating to compensation, benefits, time management and HR systems are being centrally channeled and managed through this department. HR Partners are thus enabled to focus fully on supporting line managers and employees on topics such as career counseling, people management and coaching. In the first half of 2018, a new HR Shared Service Center will be going operational in Portland. ▽

MEASURING THE SUCCESS OF OUR HR INITIATIVES

▣ Our HR function measures the success and the effectiveness of the company's efforts with regard to its people initiatives through a set of chosen KPIs. We use two people KPIs: employee experience as an internal measure and employer rankings as an external measure.

Employee engagement

We have set ourselves important goals of becoming the best sports company in the world by becoming a truly consumer-centric organization and putting our people at the heart of everything we do. When it comes to measuring whether we are living up to these ambitions, our consumers and people are the best data sources.

We are convinced that our employees' feedback will play a crucial role in our pursuit of creating a world-class employee experience so we can continue to attract and retain top talent. We can only tell if we are successful by asking our people and hence empower them to share their feedback on a regular basis. In support of this thinking, the adidas Executive Board approved the launch of 'People Pulse' for all office employees with an email account. Kicked off in June 2017, People Pulse is adidas' new approach and system platform for measuring the level of employee satisfaction with the experience adidas provides as an employer.

People Pulse allows for the monthly measurement of employeeNPS (eNPS). ▣ SEE INTERNAL MANAGEMENT SYSTEM, P. 102 The calculation logic of the eNPS score is identical with brand NPS: Based on the main question 'On a scale of 0-10, how likely are you to recommend adidas as a place to work?', the total share of detractors (responses below 7) is deducted from the total share of promoters (responses scoring 9 and 10), producing the eNPS score. This new approach as well as a new focus on collecting open-comment feedback from employees on a regular basis allowed the reduction of the questionnaire to a short pulse check of seven questions maximum, with the eNPS question at the center.

The People Pulse cadence is made up of two components:

- The eNPS question which is asked every month to allow for tracking over time
- A focus topic which changes monthly and is directly derived from the company's strategic agenda as well as the new Leadership Framework and the 3Cs. The cycle repeats itself every six months

2017 marked the creation of the baseline eNPS score which was needed to establish the measurement of KPI improvement over time, as well as to produce internal benchmarks. Research shows that external benchmarks for eNPS are not meaningful to compare the level of positive employee experience between companies as People Pulse is specifically tailored to adidas' needs as well as its Creating the New strategy and People Strategy. A direct like-for-like comparison of the adidas eNPS score to that of other companies is therefore not feasible. In line with the NPS industry standard approach, the focus lies on incremental improvement of the baseline score vs. the score for each pulse. For external benchmarking, we continue to use top employer rankings such as Glassdoor and Universum, where adidas' attractiveness as an employer is compared to that of other companies in similar

and other industries. Tracking of these external rating scores is managed by the HR Talent Acquisition team on a regular basis.

Given the above, targets that were agreed with the Executive Board for the baseline year were mainly qualitative in nature with the exception of the participation rate:

Target	Result 2017
Reporting of People Pulse results	<ul style="list-style-type: none"> – Reports with scores and anonymized comments are provided to the Executive Board as well as leaders on both Board-1 and Board-2 level. – Employees have access to the overall company results via a SharePoint workspace and our global intranet a-LIVE.
Minimum participation rate per month of 50% and accumulated participation rate of 80% at least once every six months	<ul style="list-style-type: none"> – Since its launch in June, monthly participation rates have been increasing, from 45% to around 55% in November and December. – By October, approximately 85% of eligible employees had participated in at least one monthly pulse.
Results recipients to, among others, <ul style="list-style-type: none"> – actively show leadership commitment and ownership by openly discussing People Pulse results – drive action on identified areas of improvement 	<ul style="list-style-type: none"> – Leaders partner with HR and other relevant functions to review, cascade and communicate monthly results. – Discussion with network of 'People Pulse Champions' to share best-practice examples. – One example for successful implementation of feedback is the introduction of new work-life balance measures in Greater China which resulted in significant score improvements.
Expansion of People Pulse to own retail stores and Distribution Centers before the end of 2017	<ul style="list-style-type: none"> – Pilot of People Pulse for ten retail stores in Germany and the Central Distribution Center in Rieste, Germany. – Lessons-learned meetings to define roadmap for 2018 regarding the roll-out to retail stores and Distribution Centers globally.

In addition, we measured the effectiveness of People Pulse as a tool, using the November Pulse to get employees' feedback on People Pulse itself. Positive feedback revolved around the fact that People Pulse gives employees a voice and the chance to contribute and provide feedback quickly and on a regular

basis. An area for improvement is the communication of results and the definition of actions addressing the results. The insights-to-action process will therefore become a focus area for 2018.

Employer rankings

Our 'employer of choice' status continues to garner worldwide recognition and enables us to attract, retain and engage industry-leading talent to sustain the company's success and growth. In 2017, adidas locations around the world leveraged our employer brand attributes for attraction, retention and engagement strategies. This work contributed to several Top Ten rankings worldwide, including the Glassdoor and the Focus Best Employer rankings, as well as the Candidate Experience Award EMEA/APAC (Asia Pacific). This has also helped us to attract some of the industry's top talent. ▽

PERFORMANCE MANAGEMENT

▮ To drive high performance within the company, we use a performance management approach called 'The Score'. It brings target setting and performance appraisal under one common process. Each employee is evaluated at least once a year, optionally twice, and receives performance feedback accordingly. In 2018, The Score will be replaced by '#MyBest' which is a new and holistic performance development approach combining monthly high-quality conversations between the employee and the line manager, regular upward and peer feedback options with quarterly target setting and performance evaluation. In 2017, we focused on training employees on the new approach as well as piloting #MyBest.

Wages and benefits

We are committed to rewarding our employees with compensation and benefit programs that are competitive in the marketplace. Remuneration throughout the company comprises fixed and variable monetary compensation, non-monetary rewards as well as other intangible benefits. The

cornerstone of our rewards program is our Global Salary Management System, which is used as a basis for establishing and evaluating the value of employees' positions and salaries in a market-driven and performance-oriented way. The various variable compensation and benefits components we offer our employees include:

- Bonus program – Short Term Incentive (STI) program
- Profit participation program – 'Champions Bonus' (Germany)
- Long-Term Incentive (LTI) Plan for leaders and Executive Board members
- 401-K Retirement Plan (USA) and adidas Pension Plan (Germany)
- adidas Stock Purchase Plan.

We are continuously improving our remuneration approach and are therefore investing in a number of projects and initiatives to increase significance of our remuneration programs, as well as to ensure we are investing in the right people at the right level. One of the improvements we conducted was the initiation of a new salary adjustment approach. It was applied in Germany and the US in 2017 to minimize salary differences and, more importantly, inequity of employees on the same positions and grades. It is based on a higher level of detail for external market data and addresses internal pay gaps – also helping ensure that we pay equally at the same level for female and male employees.

In addition, we improved transparency and governance for management remuneration. Analytics for our global management population provided higher transparency about actual remuneration as well as internal and external positioning of compensation and benefits packages. The aim was to ensure objective decision making for management remuneration, and to continue standardizing our pay structures. In 2017, we also rolled out a new, global Long Term Incentive Program for Senior Management. This program provides Restricted Stock Units (RSU), linked to our

Earnings per Share (EPS) targets and to our share price performance. It closely links the goals of our Senior Management with those of our shareholders – sustainable success and long-term growth – and fosters company ownership mentality. We will introduce a similar plan for the Executive Board in 2018. [SEE NOTE 27, P. 186](#)

Our subsidiaries also grant a variety of benefits to employees, depending upon locally defined practices and country-specific regulations and norms. [J](#)

DEVELOPMENT AND TRAINING

Talent and succession management

[F](#) The quality of current and future talent and leadership is key to our success. With specifically designed talent management tools, we identify talents at all levels of our company who have the potential to become future leaders or key players within the organization. In order to prepare them for more complex future roles, they participate in targeted development programs and have tailored individual development plans.

Apprenticeships and internships: Our development programs are complemented by apprenticeship and internship programs. The adidas apprenticeship offers young people who want to join our company directly out of school the opportunity to gain business experience in a two- to three-year rotation program. It includes vocational training in retail, shoe technology and IT, as well as integrated study programs in fields such as digital commerce, finance or international business. At the end of 2017, we employed 65 apprentices in Germany (2016: 63) and 37 integrated study program students (2016: 35). Our global internship program offers students three to six months of work experience within adidas. In 2017, we employed 765 interns in Germany (2016: 623).

Trainee program: The Functional Trainee Program (FTP) is an 18-month program providing graduates with an international background and excellent educational credentials the

opportunity to start a functional career within adidas. The program comprises six three-month assignments in various departments. At least one of these assignments takes place abroad. At year-end 2017, we employed 63 participants in our global FTP (2016: 49).

Succession management: Our succession management approach aims to ensure stability and certainty in business continuity. We achieve this through a globally consistent succession plan which covers successors for director-level positions and above. We conduct regular reviews to ensure individual development plans are in place to prepare successors for their potential next steps.

Employee collaboration and learning

We believe that a robust and state-of-the-art internal communication platform is essential for driving employee engagement and fostering learning as well as open collaboration within our organization. We use an enterprise collaboration platform called 'a-LIVE', which encourages employees to share knowledge, collaborate and discuss current topics. In addition, we have established an 'Ask the Management' platform on our intranet, enabling employees to openly address questions to our senior leaders.

Via a-LIVE we also offer all employees access to the Learning Campus, a state-of-the-art learning platform launched in 2014 that provides opportunities for both e-learning and knowledge sharing. Employees are able to access content 24/7 in a virtual environment. Under the Learning Campus brand we also offer in-person learning activities. Through a global implementation of our Learning Management System that continued through 2017, we have increased accessibility of employee training and development activities across the globe with a future goal of the majority of in-person and digital learning activities contributing to an employee's individual People OneView profile.

In 2017, 23,113 employees accessed our Learning Campus digitally, while 4,295 employees participated in in-person learning activities, ranging from two hours to two days in duration. In 2018, adidas core learning programs will be created to support strategic business initiatives, build capabilities connected to our 3Cs and support development of future cross-functional organizational capabilities. Input into the program offer is managed through a business needs assessment supported by our HR organization. [J](#)

WORK-LIFE INTEGRATION

[F](#) We aim to harmonize the commercial interests of the company with the professional, private and family needs of our employees. Our Work-Life Integration initiatives and programs include flexible work time and place, people development and leadership competence related to work-life integration, as well as family-oriented services. In addition to providing flexible working opportunities such as teleworking, sabbaticals and parent/child offices, we have a day-care center at our headquarters in Herzogenaurach, for example. Our office in Panama also offers financial support for day care, and our office in Amsterdam provides a contingent of day-care places.

In order to plan parental leave and re-entry in the best possible way, we have dedicated and tailored programs in place providing employees with advice at an early stage and options for their return to work, also taking into consideration flexible working hours and work locations. In Germany, for instance, we guarantee our employees on parental leave their positions, which are only filled temporarily. In the US, we give parents a special option: In addition to regular parental leave, which allows new parents to stay home for up to ten weeks with 70% of their salary, adidas offers an extra two weeks' paid parental leave for parents. Furthermore, adidas' special parental bonding leave provides parents with the possibility to stay home for up to six months within the first twelve months

after the child's birth or placement. While unpaid, it offers parents the opportunity to stay home longer and take care of their new arrival and new life together.

Starting with our company's headquarters in Germany, we introduced a new off-campus working approach in 2017. Every employee with an adidas AG contract whose working tasks can be carried out independently of campus facilities, campus equipment or personal interaction onsite is eligible to work 20% of their total working time off-campus. This new Works Council agreement is based on our belief that results can be achieved in the same quality and quantity, regardless of people's location. With this regulation we are supporting our people in working more flexibly and choosing the best work environment for the task they have at hand. ▬

DIVERSITY AND INCLUSION

▬ We believe it is crucial for the success of our company to have a very diverse workforce and individuals with different ideas, strengths, interests and cultural backgrounds. We see a great benefit in the diversity of our employees as this helps us to better fulfil the wishes and multi-faceted demands of our consumers around the world. All our employees are appreciated – regardless of gender, nationality, ethnic origin, religion, world view, disability, age, sexual orientation or identity.

At our company's headquarter, we have employees from more than 100 nations. As part of our global diversity approach we proactively pursue a portfolio of internal and external activities as well as memberships:

Internal activities

▬ We have regular events highlighting diversity as a key topic, such as our global Diversity Day. We support the 760-member strong global Women's Networking group.

Additionally, we continue our support of the international LGBTQ community, which is also driven by our employees at our major locations. 2017 also saw the creation of a new Experienced Generation network which represents the interests and needs of our more experienced employees.

▬ We provide quarterly diversity reports to management to support decision making and target setting, and provide diversity training to our employees and gender intelligence training to our leaders.

External activities and memberships

▬ Our active membership in 'Charta der Vielfalt' ('Diversity Charter'), Prout at Work and the Diversity and Inclusion in Asia Network (DIAN) allows us to promote communication and the sharing of best practices and insights.

▬ We have been participating in international diversity career fairs and events such as Women in Tech, Opportunities for Women Conference and the British LGBT awards.

▬ adidas is listed in the *genderdax* ▬ [SEE GLOSSARY](#) and regularly takes part in benchmark studies in order to review our activities in the fields of diversity and inclusion. ▬

MIXED LEADERSHIP TEAMS

▬ At adidas, we believe in mixed leadership teams as a competitive advantage and driver of success. A prerequisite for increasing the number of women at the highest levels of management is the general promotion of women within the company worldwide at all levels of management. We have various initiatives in place, e.g. with members of the Executive Board agreeing to mentor female talents as well as an equal gender split in our GHIPO program to guarantee that our succession pipeline is balanced. In addition, our women's network is also working on mentoring circles to foster the professional development of junior colleagues. Already in 2011, adidas proactively set itself the goal of increasing the number of women in management positions in the coming years. [ADIDAS-GROUP.COM/S/EMPLOYEES](https://www.adidas-group.com/s/employees)

Mixed leadership targets

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adidas AG	Target set in 2015 for 2017	Evaluation June 30, 2017	Target set in 2017 for 2019/2022
	Supervisory Board to appoint one woman to the adidas AG Executive Board	Karen Parkin appointed as the first woman to the adidas AG Executive Board in May 2017	Percentage share of women on the Executive Board by 2022: 14.29% (1/7)
	Percentage share of women in management positions (Board-1 level) to be increased from 11% (July 2015) to 18%	Percentage share of women in management positions (Board-1 level): 18%	Percentage share of women in management positions (Board-1 level) to be increased to 24% by 2019
	Percentage share of women in management positions (Board-2 level) to be increased from 26% (July 2015) to 30%	Percentage share of women in management positions (Board-2 level): 29%	Percentage share of women in management positions (Board-2 level) to be increased to 30% by 2019
Global	Target set in March 2011 for 2017	Evaluation 2017	Target set in 2017 for 2020
	Percentage share of women in management positions to be increased from 30% (March 2011) to 32%	Percentage share of women in management positions: 31%	Percentage share of women in management positions to be increased to 32%

Pursuant to the German 'Law on Equal Participation of Women and Men in Leadership Positions in the Private and Public Sector' the Supervisory Board and Executive Board of adidas AG have set specific targets to be achieved by June 30, 2017, and new targets to be achieved by December 31, 2019. [SEE CORPORATE GOVERNANCE REPORT INCLUDING THE DECLARATION ON CORPORATE GOVERNANCE, P. 33](#) [SEE TABLE 26](#)

GLOBAL EMPLOYEE POPULATION

On December 31, 2017, the company had 56,888 employees (thereof 7,581 adidas AG), which represents a decrease of 3% versus 58,902 in the previous year. This is a result of the divestiture of our TaylorMade and CCM Hockey businesses. On a full-time equivalent basis, our company had 48,775 employees (thereof 6,927 adidas AG) on December 31, 2017 (2016: 50,319). [SEE TABLE 27](#)

Personnel expenses increased to € 2.549 billion in 2017 (2016: € 2.373 billion), representing 12% of sales (2016: 13%).

[SEE NOTE 33, P. 201](#) An overview of the development of our employee base in the past ten years can be found in our ten-year overview. [SEE TEN-YEAR OVERVIEW, P. 229](#)

Employee statistics¹ 27

	2017	2016
Total number of employees ²	56,888	58,902
Total employees		
Male	50%	50%
Female	50%	50%
Management positions		
Male	69%	70%
Female	31%	30%
Average age of employees (in years)	30	30
Average length of service (in years)	4	5

¹ At year-end. Figures reflect continuing operations as a result of the divestiture of the Rockport, TaylorMade, Adams Golf, Ashworth and CCM Hockey businesses.

² Number of employees on a headcount basis.

Number of employees by function¹ 28

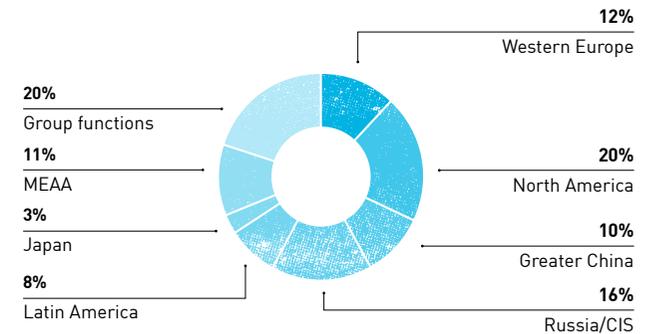
	Employees ²		Full-time equivalents ³	
	2017	2016	2017	2016
Own retail	32,698	35,109	25,640	27,552
Sales	3,795	4,018	3,680	3,910
Logistics	5,890	5,999	5,617	5,721
Marketing	5,964	5,379	5,742	5,166
Central functions and administration	5,157	5,044	4,835	4,749
Production	1,132	1,164	1,105	1,135
Research & development	1,062	1,021	1,002	955
IT	1,190	1,168	1,154	1,131
Total	56,888	58,902	48,775	50,319

¹ At year end. Figures reflect continuing operations as a result of the divestiture of the Rockport, TaylorMade, Adams Golf, Ashworth and CCM Hockey businesses.

² Number of employees on a headcount basis.

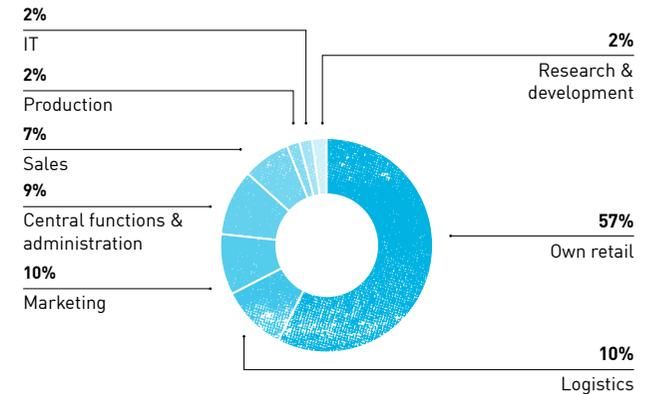
³ Number of employees on a full-time equivalent basis.

Employees by region¹ 29



¹ At year-end.

Employees by function¹ 30



¹ At year-end.

SUSTAINABILITY

Being a sustainable business is about striking the balance between shareholder expectations and the needs and concerns of our employees and consumers, the workers in our supply chain and the environment. We believe that acting as a responsible business will contribute to lasting economic success.

OUR APPROACH

Our commitment to sustainable practices rests on the company's mission: To be the best sports company in the world. Best means that we design, build and sell the best sports products in the world, with the best service and experience and in a sustainable way. This mission is supported by the adidas sustainability roadmap toward 2020 and beyond, which is a direct outcome of our business strategy 'Creating the New'. We believe that, through sport, we have the power to change lives. But sport needs a space to exist. These spaces are increasingly endangered due to man-made issues, including human rights violations, pollution, growing energy consumption and waste. Our holistic approach to sustainability responds to the challenges that endanger the spaces of sport and simultaneously our planet and people. Building on existing programs, it tackles these subjects that are most material to our business and our stakeholders, and translates our overall sustainability efforts into tangible goals for 2020 that have a direct impact on the world of sport we operate in. [ADIDAS-GROUP.COM/SUSTAINABILITY](https://www.adidas-group.com/sustainability)

MATERIAL TOPICS

We seek to ensure that we address the topics that are most salient to our business, our key stakeholders as well as the challenges ahead. To identify these topics we openly engage with our stakeholders and involve their views and opinions in

decisions that shape our day-to-day-operations. 2017 saw a refreshment of this materiality exercise. Building on the insights gained from past assessments we categorized potential relevant topics in a first step. We then validated these topics through in-depth discussions with experts across all relevant functions. In doing so, our focus centered on the importance a topic has for our business performance and stakeholders but also considered the impact adidas has on these topics. As a result we were able to confirm our strategic ambitions and embedded goals that we aim to reach by 2020.

[SEE NON-FINANCIAL STATEMENT, P. 100](#)

STAKEHOLDER DIALOGUE AND TRANSPARENCY

Engaging openly with stakeholders and establishing ways to increase transparency and disclosure has long been central to our approach. Our stakeholders are those people or organizations who affect or are affected by our operations, including our employees, consumers, suppliers and their workers, customers, investors, media, governments and NGOs. The adidas 'Stakeholder Relations Guideline' specifies key principles for the development of stakeholder relations and details the different forms of stakeholder engagement. Through active participation in, for example, the Better Cotton Initiative (BCI), the Sustainable Apparel Coalition (SAC), the Leather Working Group (LWG) and the Apparel and Footwear International RSL Management (AFIRM) Working Group, we work closely with leading companies from a variety of sectors to develop sustainable business approaches and to debate social and environmental topics on a global level. This is also supported by our membership in organizations such as the World Federation of the Sporting Goods Industry (WFSGI), the Fair Factories Clearinghouse (FFC), the Fair Labor Association (FLA) and the German government-led Partnership on Sustainable Textiles ('Textilbündnis'). In addition, we build awareness, capacity and knowledge of laws and rights among factory management and workers by partnering with leading

providers such as the EHS+ Centre in China and the International Labour Organization's (ILO) Better Work program.

[ADIDAS-GROUP.COM/S/PARTNERSHIPS](https://www.adidas-group.com/s/partnerships)

We believe transparent communication to our stakeholders is critical. For that reason we regularly disclose important sustainability updates from our work throughout the year on our corporate channels including our corporate website. A key element is the publication of our global supplier factory lists, showing factories we source from. The lists were first disclosed in 2007 and are updated twice a year. In addition, we publish lists of the factories that manufacture products for major sports events such as the FIFA World Cup or Olympic Games, and disclose the names of factories of suppliers who process materials for our primary suppliers or subcontractors, where the majority of *wet processes* [SEE GLOSSARY](#) are carried out. [ADIDAS-GROUP.COM/S/SUPPLY-CHAIN-STRUCTURE](https://www.adidas-group.com/s/supply-chain-structure)

GOVERNANCE STRUCTURE

A cross-functional governance structure ensures timely and direct execution of these programs that drive achievement of our voluntarily set goals for 2020. A Sponsor Board composed of functional heads from Social and Environmental Affairs (SEA), Global Operations (GOPS), Global Brands, Human Resources, Global Workplaces, Retail Concept, Sales, Finance and Communication oversees the progress made toward our goals in bi-monthly meetings and gives direction for further development of the sustainability roadmap. The Sponsor Board works in close alignment with the strategic working group that is tasked with the monitoring of ongoing relevant developments within the company and the reporting of progress to the Sponsor Board. Ultimately, the program owners ensure operational execution of the programs. Important updates and requests for decision making are shared with the Executive Board and designated sustainability champions on a regular basis.

EXTERNAL RECOGNITION

▣ We have continuously received positive recognition from international institutions, rating agencies, NGOs and socially responsible investment analysts for our sustainability initiatives. In 2017, adidas AG was again represented in a variety of high-profile sustainability indices and subject to corporate sustainability assessments. ▣ [SEE OUR SHARE, P. 57](#)

For example, for the 18th consecutive time, adidas AG was selected to join the Dow Jones Sustainability Indices (DJSI), the world's first global sustainability index family tracking the performance of the leading sustainability-driven companies worldwide. As one of the top-scoring companies in our industry 'Textiles, Apparel & Luxury Goods', we earned the Gold Class distinction for excellent corporate sustainability performance for the second year in a row and were rated industry best in the criteria Human Rights, Supply Chain Management, Impact Measurement and Valuation, Materiality, Environmental Policy and Management Systems, Risk and Crisis Management, Brand Management, Corporate Citizenship and Philanthropy, and Customer Relationship Management. As a result of our response to assessments conducted by the Carbon Disclosure Project (CDP), adidas was awarded with a B score in the Climate Change submission and with an A-score in the Water submission in 2017. Furthermore, adidas received recognition in the annual CITI (Corporate Information Transparency Index) 4.0 evaluation for the environmental performance of our supply chain in China for the fourth year in a row. In 2017, we ranked first in the leather industry, and fifth out of more than 200 global brands. adidas further ranked second in its industry in the Corporate Human Rights Benchmark evaluation and, for an unprecedented third time, received accreditation for its social supply chain program by the FLA. To provide information for the third accreditation, nine years of social compliance work was evaluated. Our program was first accredited by the FLA in 2005, then reaccredited in 2008. ▣ [ADIDAS-GROUP.COM/S/RECOGNITION](#)

OUR PROGRESS

For years, adidas has regularly reported about its sustainability performance by measuring and disclosing the progress made toward our targets.

PRODUCT SAFETY

▣ Product safety is an imperative. As a company we have to manage the risk of selling defective products that may result in injury to consumers or impair our image. To mitigate this risk, we have company-wide product safety policies in place that ensure we consistently apply physical and chemical product safety and conformity standards. Since pioneering the Restricted Substances Policy ('A-01' Policy) in 1998, we continue to develop policies which ban or restrict chemicals in our products. ▣ [ADIDAS-GROUP.COM/S/PRODUCT-SAFETY](#)

The A-01 Policy for product materials covers the strictest applicable local requirements and includes best-practice standards as recommended by consumer organizations. It prohibits, for example, the use of chemicals considered harmful or toxic, the sourcing or processing of raw materials from any endangered or threatened species and the use of leathers, hides or skins from animals that have been inhumanely treated, whether these animals are wild or farmed. The policy is updated at least once a year based on findings in our ongoing dialogue with scientific organizations and is mandatory for all business partners who have to confirm receipt and acknowledgement of the latest policy update each year in a written format.

Both our own quality assurance laboratories and external testing institutes are used to constantly monitor material samples to ensure supplier compliance with these requirements. Materials that do not meet our standards and specifications are rejected. To ensure successful application of the policy, we promote internal business understanding,

offer global support by developing guidelines and systems, and monitor and influence standards and regulations through external observation and interaction. Senior Management from SEA and GOPS reviews and signs off policy updates and is informed about proper execution and monitoring.

We publish our A-01 Policy annually on our corporate website and communicate it to all relevant stakeholders internally and externally. The efficiency of our product safety approach is evaluated by the absence of any product recalls as well as by benchmarking standards and executional procedures against the guidance as developed by the AFIRM Group.

Progress toward targets

In 2017, we published an updated version of our A-01 Policy on our corporate website. In addition, we created a dedicated 'Product safety and compliance' workspace on our global intranet a-LIVE that serves as a platform for all employees involved in product creation by providing them with the information required to ensure we conceptualize, develop, produce and distribute products that are in compliance with national and international regulations and best-practice standards as well as in accordance with the laws of intellectual property. The workspace offers policies, manuals and standards, as well as contact details for internal global support and best-practice sharing guidelines and training material.

We have further strengthened our collaborative approach with industry peers within the AFIRM Group. We continued to mature our programs on a global scale with enhanced supplier training tools and outreach, and contributed to a consolidated AFIRM Restricted Substances List that harmonizes a Restricted Substances Lists across the industry. We further participated in several public stakeholder consultation processes initiated by the European Commission (ECHA), and also several US state legislative initiatives to inform governmental entities on implications and opportunities of drafted legislation.

In 2017, we recorded quality issues for one accessory product (model adidas Hockey Pro Glove) with around 3,000 produced items, out of 321 million units of hardware produced during the years of manufacture. One product item identified during a spot check by Dutch authorities at a point of sale was found to be not compliant with the REACH regulation of the European Union. This subsequently led to immediate action from our end. All products that were delivered to markets were recalled by asking consumers who purchased this article to return it to the store where it was bought. We have not been notified about any consumer complaints related to this product quality deficit. ▬

ENVIRONMENTAL IMPACTS

▮ adidas is proactively addressing the impacts of climate change through a number of initiatives in its own operations, its supply chain and through various partnerships. As an example, the company joined the ‘UN Climate Neutral Now’ initiative in 2015 to promote a wider understanding of the need and the opportunities for society to become climate neutral as well as to showcase that many organizations are already taking concrete action in this direction. As such, adidas is committed to action steps as a champion of the initiative such as the continued estimation and reduction of its emissions. ▬

ORGANIZATIONAL FOOTPRINT

▮ In 2016, for the first time, we conducted a fact-based pilot analysis to assess our organizational environmental footprint. The aim was to better understand where our main environmental impacts occur along our value chain, and to translate them into monetary terms. Using the baseline of 2015, we focused on five main environmental impacts: Greenhouse Gas (GHG) emissions, water consumption, land use as well as air and water pollution. Results show that only 4% of our impact relates to our core operations (operations related to all of our administration offices, distribution centers and own production sites globally, as well

as own retail stores globally). The biggest impact however occurs in the upstream supply chain in factories beyond the Tier 1 suppliers we have a direct relationship with. ▮ SEE DIAGRAM 31 ▬

OWN SITES

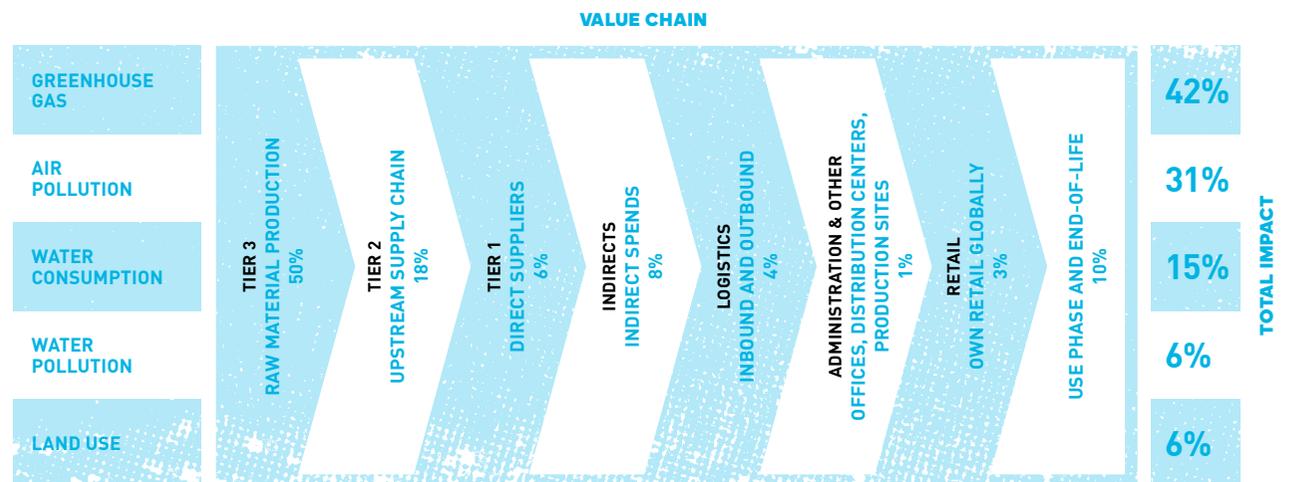
▮ Since 2008, our ‘Green Company’ program strives to achieve ambitious savings in water, waste and energy at adidas own sites globally. Including administrative offices, production facilities and distribution centers, the program covers more than 85% of our global employee base (excluding own retail). In 2015, we presented a new set of targets to be achieved by 2020, including targets for carbon reduction that were calculated considering a science-based methodology and context-based targets for water reduction.

➔ ADIDAS-GROUP.COM/S/ENVIRONMENTAL-APPROACH

Progress is tracked annually through an environmental data reporting system that allows for follow-up toward the set targets and is disclosed in detail in our annual Green Company Report that will be available as of April 2018 on our corporate website. ➔ ADIDAS-GROUP.COM/S/GREEN-COMPANY-REPORTS

In 2016, we established an Integrated Management System (IMS) which combines three existing management systems: ISO 50001 (Energy), ISO 14001 (Environment) and OHSAS 18001 (Health and Safety). IMS is helping us to drive further business integration and impact relevant decisions for our operations globally. A dedicated IMS policy helps to promote wider understanding and ensures application among all adidas entities affected. In addition, our global intranet a-LIVE supports best-practice sharing among all adidas employees globally.

Organizational footprint¹



¹ Greenhouse gas: carbon dioxide, methane and nitrous oxide. Air pollution: sulphur oxides, nitrogen oxides, particulate matter, toxic organic substances. Water consumption: i.a. surface water, ground water. Water pollution: i.a. nitrogen and phosphorus, toxic organic substances, heavy metals. Land use: arable land, pastures and grassland, industrial land use, unsustainable forest area.



Progress toward targets

By the end of 2017, our own sites globally managed a 29% reduction in carbon net emissions (baseline 2015) and a 27% reduction in water consumption per employee (baseline 2008).

Targets 2020	2017	2016
3% absolute annual reduction in CO ₂ Scope 1 and Scope 2 ¹ net emissions (baseline 2015)	29%	11%
35% reduction in water consumption per employee (baseline 2008)	27%	23%

¹ Scope 1: Emissions that arise directly from sources that are owned or controlled by adidas entities, such as fuels used in our boilers, Scope 2: emissions generated by purchased electricity consumed by adidas entities.

Three of our facilities received **LEED**  **SEE GLOSSARY** Gold certification. After the office in Santiago, Chile, received certification in 2016, the new office in Buenos Aires, Argentina was the second office in South America to be awarded with this certification. The India headquarters in Gurugram became our first LEED Gold certification in Asia and the relocated headquarters in Dubai also became LEED Gold certified. In addition, adidas received its first-ever LEED certification for own retail. The store in Madrid was accredited for its interior design and construction.

In line with our ambition to reduce the environmental footprint of our consumer events by 2020, we developed our first 'Sustainable Events' guidelines which will serve as orientation for our markets globally to run events more sustainably and inspire best-practice sharing opportunities. The guidelines are available to our internal teams through a-LIVE and to external agencies, with the aim of, for example, increasing energy awareness and minimizing the use of single-use plastic at our own events.

2017 also experienced renewed and visible support for our ambition to further reduce our environmental footprint from the adidas Executive Board, who challenged all adidas facilities worldwide to remove single-use plastic items that are disposable and generally used only once before they are thrown away, such as plastic bags, water bottles and cutlery. The changes will avoid more than 40 tonnes of single-use plastic per year. The announcement that was made on a-LIVE was the most successful post to date, showing the high commitment and engagement of both our Senior Management and employees worldwide toward responsible business practices. 

SUPPLY CHAIN

 As almost all of our production is outsourced, a significant part of our environmental impact occurs, at different intensities, throughout the supply chain. Therefore, for us, sourcing is not only about ensuring high product quality and timely delivery, it also means working with our suppliers to ensure the highest environmental standards and supporting them to reduce their overall water consumption and waste volume as well as improve their carbon footprint. Using the environmental performance of our own sites as best-practice examples, we provide a set of specific policies and guidelines to our suppliers: Mandatory for all business partners, the 'Workplace Standards' (the supply chain code of conduct) as well as supportive guidelines such as our 'Environmental Guidelines' and 'Guide to Best Environmental Practice' are updated regularly and build the basis for our engagement with suppliers. In addition, we have initiated a system of multi-level and cross-functional training sessions with our global supplier network and provide regular training. Guidance and training materials are reviewed by SEA Senior Management prior to release. [ADIDAS-GROUP.COM/S/SUPPLY-CHAIN-APPROACH](https://www.adidas-group.com/s/supply-chain-approach)

One of the ways we try to minimize our suppliers' environmental impacts at their manufacturing plants is by helping them establish sound environmental management systems. The majority of our footwear sourcing volume, 95% (2016: 96%), is produced in factories which are certified in accordance with the International Environmental Standards ISO 14001 and/or the Workplace Health and Safety Management Standards OHSAS 18001. The remaining part of our footwear sourcing volume is produced in factories that have other management systems in place. All footwear factories in our monitoring scope are regularly assessed against our standards on environment and workplace health and safety, receiving evaluation by means of our environmental compliance E-KPI rating.

Environmental compliance (E-KPI)

E-KPI is our tool designed to measure and improve environmental performance of our strategic Tier 1 suppliers by setting them 20% intensity reduction targets to be achieved by 2020 in the areas of energy, water and waste (baseline 2014). Using a benchmarking approach, E-KPI allows for a high level of transparency into suppliers' actual consumption intensity, supporting us to define suppliers' specified areas for improvement and training needs that match their respective situation. We follow a similar approach for our apparel material Tier 2 suppliers, with the aim of them achieving a 35% water reduction by the end of 2020 (baseline 2014)¹.

Progress toward targets

Compared to the 2016 results, our suppliers enrolled in our environmental program made good progress². 48% of strategic suppliers are on track to achieve their energy reduction target for 2020, which represents an increase of 11 percentage points compared to the results from the previous measurement. More than half of these suppliers (55%) are on track to

¹ Apparel material suppliers are specialists in printing and dyeing operations. Based on results from previous years and a change in our tracking methodology, the target for our apparel material suppliers was adjusted to a 35% reduction by 2020.

² E-KPI 2017 refers to environmental data covering full year 2016, using a baseline of 2014. Strategic suppliers enrolled in our environmental program cover more than 80% of our total sourcing volume.

achieve their waste reduction target, also marking a significant improvement of 16 percentage points compared to the previous results. 54% of this group of suppliers are on their way to achieving the water reduction targets, showing a stable performance and no change in percentage points compared to the previous ratings. In addition, 46% of our apparel material suppliers made good progress and are well on their way to achieve the 2020 target.

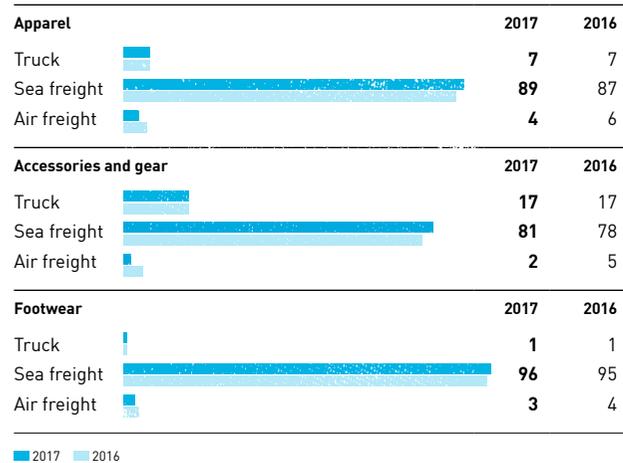
If facilities' performance achievement is at risk, we take several steps to support and ensure their performance gets back on track. For example, in 2017, we launched various energy efficiency projects targeting underperforming facilities in Vietnam, Cambodia and Indonesia with the help of external

expertise that identified and outlined short- and medium-term action for the facilities with a positive impact either immediately or within the next three years. Similarly with waste, we did a pilot assessment in Vietnam to identify waste reduction and recycling opportunities. The global guidelines developed will support all facilities to manage their waste and identify opportunities to recycle. Low-performing facilities are further asked to develop improvement plans and provide regular progress updates. adidas also hosts joint discussions with the factories.

In 2017, we tracked again the environmental impact related to the transport of our goods and recorded a small reduction in air freight and a slight increase in sea freight throughout all categories, while truck freight remained stable. All in all, the vast majority of our shipments take place via sea freight.

SEE DIAGRAM 32

Freight types used to ship adidas and Reebok products¹ in % of product shipped 32



¹ Figures are expressed as a percentage of the total number of products transported. Data covers products sourced through Global Operations, excluding local sourcing.

SUSTAINABLE MATERIALS AND PROCESSES

Following our ambition to create the best for the athlete while optimizing our environmental impact, we innovate materials and processes. We are committed to steadily increasing the use of more sustainable materials in our production, products and stores and are driving toward closed-loop solutions. Our approach to sustainable materials is influenced by new technological trends and developments, engagement with stakeholders including scientific organizations as well as market availability. Any major changes in the material selection that impact product costs are subject to review and approval by Senior Management. Execution and progress is tracked and managed by the respective materials development and sourcing departments.

As a founding member of the Better Cotton Initiative (BCI), adidas is working on reducing the use of conventional cotton

and has committed to increasing the sourcing volumes of Better Cotton, with the aim of achieving 100% *sustainable cotton* SEE GLOSSARY by 2018. Not only does the BCI aim to reduce the use of pesticides, it also promotes efficient water use, crop rotation and fair working conditions.

In addition, we aim to reduce the use of virgin plastic and are increasing the use of recycled polyester in our products. As of 2015, adidas has partnered up with *Parley for the Oceans* SEE GLOSSARY. As a founding member, adidas supports Parley for the Oceans in its education and communication efforts and commits to the Parley A.I.R. (Avoid, Intercept, Redesign) strategy. As part of this strategy we are working on turning what we believe is a problem (marine plastic pollution) into progress with an eco-innovative replacement for virgin plastic, *Parley Ocean Plastic* SEE GLOSSARY, and have committed to extend the supply chain for Parley Ocean Plastic. SEE INNOVATION, P. 78 SEE CORPORATE STRATEGY, P. 62 ADIDAS-GROUP.COM/S/SUSTAINABILITY-INNOVATION

We are further rolling out a global take-back program to all our key cities and markets, implementing 'Make every thread count', with the main objective to raise consumers' awareness of what happens to products at the end of their life. It helps consumers to give their old clothes and footwear a second life. Consumers can drop off old shoes and apparel from any brand. The collected items are then sent to the adidas Distribution Center, where they are picked up by a service provider that sorts products according to different quality criteria. Products either go into a second-hand market or are further recycled into secondary raw material, to be used for new products in various industries. A small portion of products (less than 10%) cannot be recycled and thus is sent for disposal. ADIDAS-GROUP.COM/S/PRODUCT-END-OF-LIFE

Progress toward targets

In 2017, 93% (2016: 68%) of the cotton we sourced globally was Better Cotton, exceeding our original target of 80%. This is a huge step toward our goal of sourcing 100% sustainable cotton by 2018. Our success is the result of clear target setting – both with suppliers and with internal teams who support the sourcing of Better Cotton for our products.

	2015	2016	2017
Better Cotton sourced	43%	68%	93%

We already eliminated plastic bags in our own stores globally in 2016, and have started to integrate Parley Ocean Plastic into key products, including running, outdoor, Originals and Stella McCartney shoes, football jerseys and swimwear. ADIDAS.COM/PARLEY Overall, we managed to create more than one million pairs of shoes with Parley Ocean Plastic in 2017. Together with Parley for the Oceans, we have further driven the conceptualization of the required set-up for a global collection network at scale. As part of our overall effort to extend social and environmental monitoring to lower tiers, we expanded our scope for the Parley supply chain from apparel suppliers to also include suppliers for footwear, and accessories and gear, now covering almost 20 Tier 2 suppliers in total.

Our ambition to expand the use of waterless dyeing technologies for our products received renewed support in 2017 as it was chosen as a key accelerator project going forward. This means that we will look into different technologies, including DryDye, with the aim to develop a holistic approach on how to save water overall, including water reduction during pre-treatment or the creation of a closed-loop water treatment system in dyeing factories. Furthermore, we also built on and

advanced our existing take-back program in Canada and introduced 'Make every thread count' to four of our strategic key cities (Los Angeles, New York, London and Paris). [↵](#)

CHEMICAL MANAGEMENT

For years, adidas has been running leadership programs in Chemical Management within its area of direct influence. In a spirit of continuous improvement of our chemical footprint, these programs are regularly updated. Our approach has been developed in consultation with external stakeholders including chemical experts, environmental organizations and industry federations and was reviewed by the Sponsor Board and finally approved by SEA and GOPS Senior Management. Our targets for 2020 include achieving 100% sustainable input chemistry by adopting the Manufacturing Restricted Substances List (MRSL) of the Zero Discharge of Hazardous Chemistry (ZDHC) group, phasing out hazardous chemicals and providing our strategic suppliers with a list of positive chemistry (the bluesign bluefinder).

ADIDAS-GROUP.COM/S/CHEMICAL-FOOTPRINT

Progress toward targets

In 2017, we collected the ZDHC MRSL acknowledgement letters from our suppliers, with more than 99% signed letters received from our strategic suppliers. Carefully reviewing the feedback from our suppliers will support us to define proper tracking and monitoring of MRSL compliance in our supply chain. On our way to phasing out hazardous chemicals, we successfully delivered against our commitment to be 99% free of poly- and perfluorinated substances (PFCs) by no later than the end of 2017: More than 99% of the adidas products for the spring/summer 2018 season will be PFC-free. Lastly, our suppliers exceeded the 2017 targets of 50% of auxiliaries and 80% dyestuffs to be bluesign-approved: By 2020, our

strategic apparel material suppliers will have 80% of auxiliaries and 90% of dyestuffs bluesign-approved.

	2014	2017
Products free of PFC	90%	> 99%

Volatile Organic Compounds (VOCs), which are typically found in solvents used in our manufacturing process, can – in high concentration – cause breathing difficulties and other health problems for production workers. In 2017, we achieved an all-time low of 11.6 grams (2016: 14 grams) of VOCs per pair of shoes³. By applying innovative as well as environmentally sound bonding and priming technologies while following the adidas guidelines on the use of chemicals, our athletic footwear suppliers have been able to reduce the use of VOCs from well above 100 grams per pair in 1999 to below 12 grams. [↵](#)

FAIR WORKING CONDITIONS IN OUR SUPPLY CHAIN

adidas recognizes its responsibility to respect human rights and the importance of showing that we are taking the necessary steps to fulfil this social obligation as a business. We do this by striving to operate responsibly along the entire value chain, by safeguarding the rights of our own employees and those of the workers who manufacture our products through our Workplace Standards, and by applying our influence to affect change wherever human rights issues are linked to our business activities. As part of its human rights efforts, adidas has developed a modern slavery outreach program that looks beyond strategic Tier 1 suppliers, aiming to drive greater transparency in its supply chain.

ADIDAS-GROUP.COM/S/HUMAN-RIGHTS

³ Data covers production in our main sourcing region Asia.

Ensuring compliance with standards

Since its inception in 1997, our human and labor rights program for our supply chain has been built on the back of intense stakeholder outreach and engagement, seeking to understand and define the most salient issues to address as a company. Our Workplace Standards, the supply chain code of conduct established in 1997, are a contractual obligation under the manufacturing agreements the company signs with its main business partners to ensure workers' health and safety and provide provisions to ensure environmentally sound factory operations. These standards follow International Labour Organization (ILO) and United Nations (UN) conventions relating to human rights and employment practices, as well as the model code of conduct of the World Federation of the Sporting Goods Industry (WFSGI). Specific reference to the code provisions of the ILO conventions is provided in the adidas 'Guidelines on Employment Standards'. The SEA Senior Management reviews and approves all policies and implementation processes of the labor rights program.

To enforce compliance with these standards and rate suppliers on their ability to deliver fair, healthy and environmentally sound workplace conditions, adidas regularly conducts announced and unannounced, internal and external audits using a rating system with C- (social compliance) and E- (environmental compliance) KPIs and attached scores between 1C/1E and 5C/5E (with 1 being the worst and 5 being the best). According to the results, our sourcing teams decide the course of action, ranging from training needs at the factories to reinforcement mechanisms such as sending warning letters or even termination of contracts. Potential new suppliers are assessed in a similar way and orders can only be placed if approval by the SEA team has been granted.

Worker empowerment

We offer any stakeholder the opportunity to anonymously raise complaints and have found efficient ways to specifically empower workers in our supply chain by providing them with innovative tools to raise their voice. [➔ ADIDAS-GROUP.COM/S/SUSTAINABILITY-CONTACT](https://www.adidas-group.com/s/sustainability-contact) Since 2012, in parallel to existing grievance systems, the 'Worker Hotline' enables factory workers to anonymously ask questions or raise concerns by writing a text message. Additional ways to measure worker satisfaction and get their view are worker satisfaction surveys that we started to conduct in Indonesia in 2016.

Our ambitions for 2020 include achieving 100% of strategic suppliers⁴ covered by innovative grievance mechanisms and supporting our suppliers and licensees in further improving their social and environmental compliance performance as measured by our C- and E-KPI rating tools.

Progress toward targets

Throughout 2017, we deepened our stakeholder engagement on the topic of human rights, extending our outreach to representatives of special-interest groups, migrant workers, and other vulnerable communities. We continued our involvement with a UN-backed multi-stakeholder committee, examining the adverse human rights impacts of mega sporting events and supported the UN's Standards of Conduct for Business on LGBTI rights. Our engagement with the newly formed Business Network for Civic Freedoms and Human Rights Defenders included, for example, responding to calls from labor rights advocates for direct engagement with the Cambodian government over freedom of expression and association. We further contributed to the UN Special Rapporteur's fourth annual report on the situation of human rights defenders and spoke at the United Nations in Geneva on this very topic. In addition, together with other stakeholders,

we have maintained a seat on FIFA's Independent Advisor Board on Human Rights.

Efforts within our modern slavery outreach program have ranged from providing targeted training to almost 100 Tier 2 suppliers across Asia to gaining deeper insights into prevailing labor conditions at the Tier 3 raw material source for leather and cotton. We were recognized as a leading brand in the KnowTheChain ranking that examined forced labor risks in the leather supply chain in 2016 and were awarded the Thomson Reuters Foundation Stop Slavery Award 2017, which celebrates businesses that excel in efforts to identify, investigate and root out forced labor from their supply chains.

We were able to expand the Worker Hotline service: 63% of our strategic suppliers with more than 250,000 factory workers across four of our major sourcing countries (Cambodia, China, Indonesia and Vietnam) were covered by the end of 2017. Our focus was to improve this service to develop into a digital worker grievance platform, including a new app-based version which was piloted in some factories. We also further rolled out the worker satisfaction survey to a total of 47 factories across nine countries with around 8,000 factory workers participating in the survey. The results will help our suppliers to identify areas for improvement that need to be addressed, with progress to be communicated back to the workers. Lastly, we saw more than two thirds of our strategic supply chain evaluated with a 3C rating and good performance. More details are provided below. [➔](#)

⁴ Strategic suppliers are responsible for around 80% of our global production volumes.

OUR PERFORMANCE (SUPPLY CHAIN)

At the end of 2017, we worked with 782 (2016: 1,038) independent factories which manufacture products for our company in 56 countries (2016: 63). [SEE DIAGRAM 33](#) The main reason for the decline in the number of suppliers is the divestiture of the TaylorMade and CCM Hockey businesses as well as further consolidation at factories producing for our Sports Licensed business in 2017. We worked with 62 licensees whose suppliers manufactured products in 360 factories across 44 countries (2016: 61 licensees in 377 factories across 48 countries). 68% of the factories are located in the Asia Pacific region, 20% in the Americas, and 12% in Europe, Middle East and Africa (EMEA)⁵. [SEE TABLE 33](#)

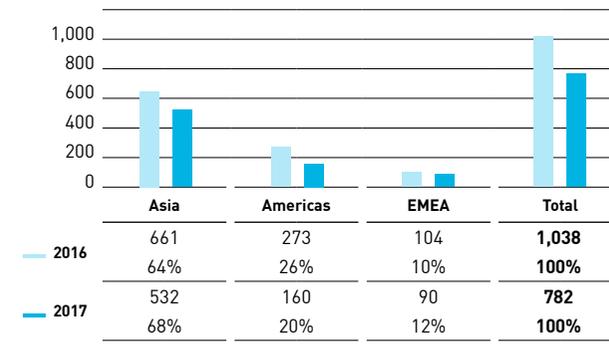
AUDITS

In 2017, adidas conducted 1,015 social compliance and environmental audits (2016: 989), using in-house technical staff as well as external third-party monitors commissioned by adidas business entities and licensees. [SEE TABLE 34](#) [SEE TABLE 35](#)

In addition, 114 self-governance audits and collaboration audits were conducted. When a factory reaches a compliance maturity level of 4C and above, we empower the supplier to conduct their own audit and develop appropriate remediation plans ('self-governance' audit) while we carefully track this process. Collaboration audits are conducted in partnership with other brands, or as part of joint remediation exercises.

Supplier factories by region¹

33



¹ Excluding own factories and licensee factories.

Number of audits in supplier factories 2015 – 2017

34

	2017	2016	2015
adidas	409	372	524
External monitor	606	617	611
Total	1,015	989	1,135

Initial assessments, performance audits and environmental audits

In 2017, we conducted a total of 209 initial assessments (2016: 213), 81% of which were undertaken in Asia (2016: 84%), with China accounting for 42% of these assessments (2016: 46%). Overall, 29% (2016: 39%) of all candidate factories either were rejected outright or were rejected for failure to remediate threshold issues in a timely manner. The total number of initial assessments, the first approval stage for new entry factories, decreased marginally by 2% compared to 2016. Performance audits at our current suppliers showed a slight increase of 3%. As part of our divestiture strategy, we increased the number of audits carried out at the factories making for the brands that we divested in 2017. We did so to ensure workers received their full benefits and entitlements during the transition of the owner relationship. The total number of environmental audits increased by 8% compared to the previous year, mainly due to the increase in SAC HIGG environmental assessments. [SEE TABLE 35](#)

The number of audits in factories manufacturing goods for licensees remained the same, in line with the stable number of licensees. [SEE TABLE 36](#) The number of self-governance and collaboration audits at licensee factories totaled 26 at the end of 2017. [SEE TABLE 36](#)

AUDIT COVERAGE

A total of 48% (2016: 40%) of all active suppliers were audited in 2017. 'High-risk' locations in Asia⁶, the major sourcing region of adidas, received extensive monitoring in 2017 with an audit coverage that was close to 70% (2016: 65%). As a general principle, factories located in low-risk countries (i.e. with strong government enforcement and inspectorate systems) are considered out of scope for our audit coverage. [SEE TABLE 37](#)

⁵ Factories in scope: Individual facilities of direct supply chain including subcontractors and factories of agencies (indirect supply chain). Supplier factories: Excluding own factories and licensee factories. Licensee factories: This may include factories that produce both for adidas directly and for licensees/agents.

⁶ High-risk locations in Asia include China, Hong Kong, Macao, Vietnam, Bangladesh, Cambodia, India, Indonesia, Laos, Malaysia, Myanmar, Pakistan, Philippines, Singapore, Sri Lanka and Thailand.

AUDIT RESULTS

▣ We audit our suppliers regularly against our Workplace Standards and rate them according to their social and environmental compliance performance with a C- and E-KPI rating tool. An evaluation of E-KPI is contained in the description of the environmental performance of our supply chain.

Social compliance (C-KPI)

In 2017, more than two thirds (69%) of our direct suppliers completely fulfilled our basic expectations and received ratings of 3C or better. Out of these, 19% were given a rating of 4C or better, which reflects an increase of 3 percentage points compared to the previous year. Suppliers rated with a 4C are classified as 'self-governance', indicating that these factories have reached a high level of compliance maturity with the existence of effective social and health and safety management systems and the ability to conduct their own audits and develop remediation plans on their own.

▣ SEE DIAGRAM 37

Since 2013, there has been a focused effort to improve the 2C factories and move them up a level, which has led to a 14% reduction of suppliers in this category. The number of 1C category suppliers, which represent the lowest-performing factories with serious issues and very weak commitment to compliance, decreased from seven to six factories in 2017. Such factories are given a one-year grace period to move up a grade or have their services terminated.

The number of factories that are subject to C-KPI ratings has remained relatively stable at around 47% of the global supply chain for the last three years (2016: 45%). These factories represent our long-term strategic partners. ▣

Number of audits by region and type

35

Region	Initial assessment ¹		Performance audit ²		Environmental audit ³		Total	
	2017	2016	2017	2016	2017	2016	2017	2016
Asia	170	178	544	524	138	137	852	839
Americas	9	23	70	75	12	0	91	98
EMEA	30	12	37	34	5	6	72	52
Total⁴	209	213	651	633	155	143	1,015	989

¹ Every new supplier factory has to pass an initial assessment to prove compliance with the Workplace Standards before an order is placed. The data includes both 'initial assessments' and 'initial assessment follow-ups'.

² Audits conducted in approved supplier factories.

³ Includes SAC HIGG as well as environmental and chemical management audits.

⁴ Includes audits done in licensee factories.

Number of audits conducted in licensee factories¹

36

Region	Initial assessment ²		Performance audit ³		Environmental audit		Total	
	2017	2016	2017	2016	2017	2016	2017	2016
Asia	49	54	187	182	11	12	247	248
Americas	1	6	18	20	1	0	20	26
EMEA	3	2	16	12	1	2	20	16
Total	53	62	221	214	13	14	287	290

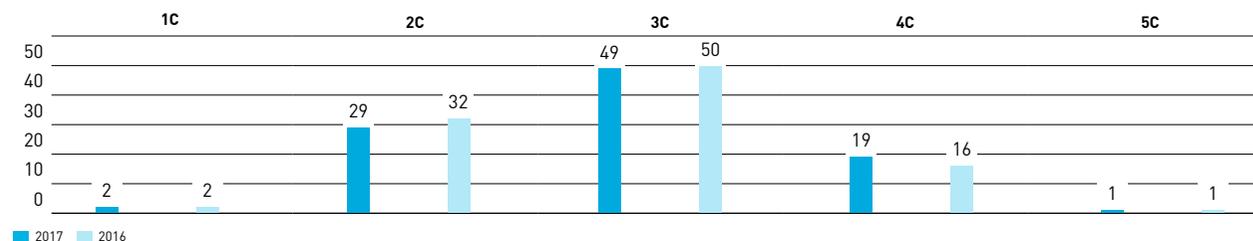
¹ This may include factories that produce both for adidas directly and for licensees/agents.

² Every new factory has to pass an initial assessment to prove compliance with the Workplace Standards before an order is placed.

³ Audits conducted in approved factories.

Percentage of KPI assessed factories by C rating

37



¹ The calculation method reflects actual supplier performance by calculating numbers using the latest KPI assessment rating of each active supplier.

VISITS AND TRAINING

During 2017, 1,241 factory visits (2016: 1,226) were undertaken. These visits involved various types of audit, Strategic Compliance Plan discussions, project work and project meetings with factory management on high-priority issues at different levels in our supply chain. Additionally, we conducted 132 training sessions and workshops for suppliers, licensees, workers and adidas employees (2016: 169). [SEE TABLE 38](#) The 22% decrease in the number of training sessions is a result of our advisory staff spending more time on engagement processes, including the development of worker satisfaction surveys and digital grievance systems for workers. In total, 1,907 people (2016: 3,349) attended the training sessions, which covered basic as well as long-term strategic topics.

NON-COMPLIANCE IN ACTIVE FACTORIES

Our suppliers are evaluated against a number of critical compliance issues. While threshold issues are serious but correctable non-compliances that can be addressed in a specified timeframe through remedial action, zero tolerance issues – such as forced labor, child labor practices and critical life-threatening health, safety and environment conditions – immediately trigger a warning and potential disqualification of a supplier. The diagrams [SEE DIAGRAM 39](#) [SEE DIAGRAM 40](#) illustrate the non-compliance findings that were identified through performance audits, collaboration audits and self-governance assessments.

Labor non-compliance findings

[DIAGRAM 39](#) presents the most frequent labor-related non-compliances identified during audits of our existing supplier factories. More than two thirds of these findings fall into the top three categories: ‘Basic wage’, ‘Management systems for working hours’ and ‘No standardized filing systems’. Besides identifying non-compliances with our Workplace Standards, adidas’ compliance team focuses on the use and effectiveness of the factories’ HR management systems, and identifies any gaps in policies and procedures related to specific risk areas, such as forced labor, child labor, freedom of association or discrimination. As a result, the percentages shown indicate the systemic shortcomings of active suppliers, rather than the confirmed presence of a specific case of non-compliance.

[SEE DIAGRAM 39](#)

Number of training sessions by region and type ¹

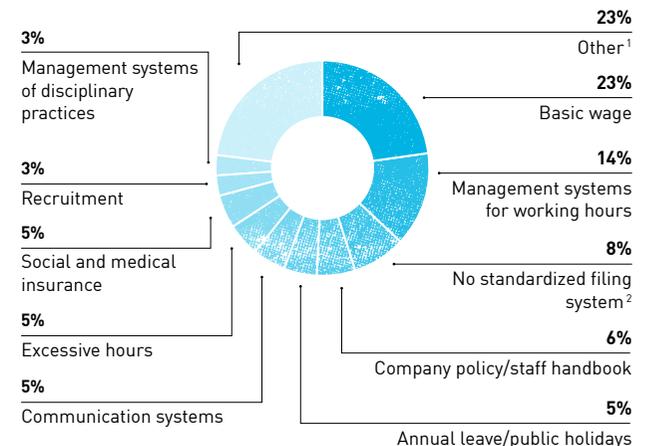
38

Region	Type and number of training sessions							
	Fundamental ²		Performance ³		Sustainability ⁴		Total	
	2017	2016	2017	2016	2017	2016	2017	2016
Asia	42	42	4	40	49	45	95	127
Americas	24	24	0	0	1	0	25	24
EMEA	7	11	2	5	3	2	12	18
Total	73	77	6	45	53	47	132	169
in %	55	45	5	27	40	28	100	100

1 Training sessions conducted for suppliers, workers, licensees, agents and adidas employees.
 2 Fundamental training covers Workplace Standards and SEA introduction, FFC training as well as SEA policies and standard operating procedures (SOPs).
 3 Performance training covers specific labor, health, safety and environmental issues.
 4 Sustainability training covers sustainable compliance guideline and KPI improvement as well as factory self-audits.

7 Data refers to the period May to December 2017 and includes self-governance and collaboration audits.

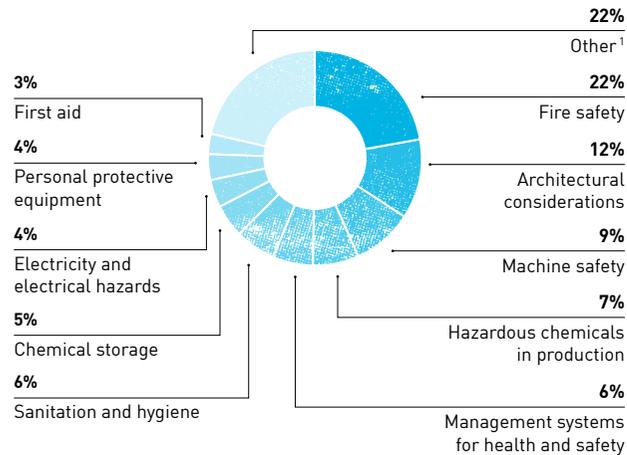
Top 10 labor non-compliance findings identified during audits in 2017 39



1 ‘Other’ includes freedom of association issues, discrimination, lack of training, etc.
 2 ‘No standardized filing system’ indicates a factory does not keep relevant information/documents and records which demonstrate compliance with laws and regulations.

Top 10 health and safety non-compliance findings identified during audits in 2017

40



¹ 'Other' refers, for example, to occupational hazard risks, personal protective equipment, ergonomics and housekeeping.

Health and safety non-compliance findings

DIAGRAM 40 shows the health and safety non-compliances identified during audits in supplier factories. Fire and electrical safety are critical areas for existing suppliers and together accounted for 26% of the non-compliances identified in 2017. The way chemicals were stored and used, including the presence of banned chemicals, accounted for 12% of non-compliance findings reported. A further 6% of the findings related to management systems, policies and procedures, and specifically a lack of compliance with our Workplace Standards and expectation for effective health and safety systems, including the recruitment and retention of qualified safety staff.

SEE DIAGRAM 40

INDEPENDENT FLA AUDITS

In 2017, the FLA conducted four factory assessments or remediation verification exercises in Guatemala, Indonesia, Cambodia and Vietnam using the methodology from the Sustainable Compliance Initiative (SCI). The number of conventional independent monitoring visits conducted by FLA accredited monitors has declined over the years for companies' programs accredited by the FLA. This shifts companies' activities from conventional monitoring activities to engagement in value-added FLA projects that focus on reducing and eliminating chronic non-compliance issues or improving monitoring methodologies. During 2017, adidas' so-called twelve redirect activities included project activities for migrant worker protection, compliance beyond Tier 1 suppliers, civil society engagement in the Americas region, and responsible sourcing practices. We continued active support of the implementation of the FLA Fair Compensation Strategy with wage data gathering exercises in Honduras, Ukraine and Cambodia.

In 2017, the FLA accredited the adidas program for the third time. To provide information for the accreditation, nine years of social compliance work was evaluated, reviewed and verified, including factory assessments, annual reports, third-party complaints, participation in strategic projects for forced labor, migrant workers' protection, fair compensation, remediation, workplace standards alignment, responsible sourcing practices, and collaboration with civil society and brands. The accreditation recognized adidas' leadership to coordinate brand efforts which address labor violations, and included commendation for the application of mobile technology to implement the text message- and application-based platform for workers to submit grievances, for the pioneering and piloting of various methods to address fair compensation for workers as well as for the programmatic implementation of social compliance standards, assessments and risk mapping beyond the Tier 1 supply chain. FAIRLABOR.ORG

ENFORCEMENT

Warning letters are an essential part of our enforcement efforts and are triggered when we find ongoing serious non-compliance issues that need to be addressed by our suppliers. We work closely with our suppliers to help them improve their performance. However, where we face situations of severe or repeated non-compliance, we do terminate business relationships with suppliers.

Warning letters

In 2017, we issued a total of 42 (2016: 31) warning letters across 15 countries. The largest number of warning letters continues to be issued in Asia, where more than 60% of all supplier factories are located. Compared to the previous year, the overall number of first warning letters doubled, mainly due to the fact that factories were not able to fully remediate their threshold issues identified in 2016, or had new threshold issues in 2017.

The total number of second warnings decreased in 2017, with three letters being issued (2016: 7). Suppliers who receive second warning letters are only one step away from being notified of possible termination of the manufacturing agreement and receive focused monitoring by the SEA team. The number of third warning letters issued to business partners (which result in factory terminations) decreased to one in 2017 (2016: 5). SEE TABLE 41

It is difficult to generalize about the grounds for a warning letter as it may be issued for a single unresolved non-conformance or for multiple breaches of our standards. The range of issues that resulted in warning letters in 2017 included non-compliances in regard to fire safety practices, receipt of wages, social and medical insurance, hazardous chemicals management, overtime, deductions, transparency and safety controls in high-risk areas.

Terminations

In 2017, we terminated agreements with four suppliers for compliance reasons (2016: 10), mainly due to non-remediated threshold issues in consecutive audits, although in one of the cases it was triggered by the supplier refusing to grant the SEA team access to audit the factory. [SEE TABLE 43](#) While terminations happen at our existing factories, we pre-screen all new factories and if our initial assessments uncover zero tolerance or threshold issues suppliers are rejected.

In 2017, initial assessments were conducted in 209 factories (2016: 213 factories), and 50 factories (2016: 71 factories) were

either rejected directly after the initial assessment identified zero tolerance issues, or were 'rejected with a second visit' due to identification of one or more threshold issues, which means they were rejected but given the chance to remediate the non-compliance issues within a specific timeframe. [SEE TABLE 42](#)

Overall, at the end of 2017, the 'first-time rejection rate' of 29% of all new factories visited was lower than the previous year (2016: 39%) and the 'final rejection rate' was at 2% (2016: 4%). [SEE TABLE 42](#) This shows the importance and impact of pre-approval screening, as well as the efforts undertaken by the suppliers to resolve issues and come into conformance with

our Workplace Standards. The remediation of factory issues is beneficial for workers as it raises the bar in terms of better and timelier pay, improved benefits, reduced hours, and the legal protection of formal employment contracts as well as significant improvements in basic health and safety within the workplace. Suppliers who have threshold issues are normally given three months to remediate those issues before being re-audited for final SEA acceptance. [J](#)

Number of warning letters issued to adidas suppliers by region¹

41

Region	1st warning		2nd warning		3rd and final warning		Total warning letters	
	2017	2016	2017	2016	2017	2016	2017	2016
Asia	35	18	1	5	0	4	36	27
Americas	2	1	1	1	0	1	3	3
EMEA	1	0	1	1	1	0	3	1
Total	38	19	3	7	1	5	42	31

¹ Including warning letters issued by licensees and agents, but excluding warnings to main suppliers for the non-disclosure of subcontractors, which are either issued directly through business entities, or by the adidas Legal department where there is a breach of contract obligations under a manufacturing agreement. A third and final warning results in a recommended termination.

Worldwide rejections after initial assessment due to compliance problems

42

	2017	2016
Total number of first-time rejections ¹	50	71
First-time rejection rate	29%	39%
Total number of final rejections ²	4	8
Final rejection rate	2%	4%

¹ Factories that were directly rejected after first visit, i.e. with no chance of being visited a second time, and factories that were rejected after initial assessments but which were given a chance for a second visit.

² Factories that were directly rejected after first visit, i.e. with no chance of being visited a second time, and factories that were rejected after being visited a second time.

Number of business relationship terminations due to compliance problems

43

Region	2017	2016
Asia	4	7
Americas	0	2
EMEA	0	1
Global	4	10

NON-FINANCIAL STATEMENT

In accordance with §§ 315b, 315c HGB in combination with §§ 289b to 289e HGB, adidas publishes a combined non-financial statement for adidas AG and the Group in this combined Management Report. The content of the non-financial statement can be found throughout the entire combined Management Report, with relevant parts being indicated by this symbol . These parts are not covered by the Audit of the Consolidated Financial Statements and of the Group Management Report, as they were subject to a separate limited assurance engagement of KPMG AG Wirtschaftsprüfungsgesellschaft.  [SEE INDEPENDENT AUDITOR'S ASSURANCE REPORT, P. 226](#) Links and references are not part of the non-financial statement and have therefore not been assessed.

adidas applied the Global Reporting Initiative (GRI) guidelines as an external reporting framework. The content of the non-financial statement combined with further information in this report and on our corporate website fulfills the GRI G4 'Core' option. The GRI content index can be found online. [➔ ADIDAS-GROUP.COM/S/REPORTING-APPROACH](#)

Description of business model

 [SEE SALES AND DISTRIBUTION STRATEGY, P. 72](#)

 [SEE GLOBAL OPERATIONS, P. 74](#)

Environmental approach

— Sustainable materials and processes

 [SEE SUSTAINABILITY, P. 88](#)

— Water consumption (supply chain)

 [SEE SUSTAINABILITY, P. 88](#)

— Carbon footprint (supply chain)

 [SEE SUSTAINABILITY, P. 88](#)

— Waste volume (supply chain)

 [SEE SUSTAINABILITY, P. 88](#)

Product responsibility

— Product safety and transparency

 [SEE SUSTAINABILITY, P. 88](#)

People and Culture

— Wages and benefits

 [SEE PEOPLE AND CULTURE, P. 81](#)

— Development and training

 [SEE PEOPLE AND CULTURE, P. 81](#)

— Employee engagement

 [SEE PEOPLE AND CULTURE, P. 81](#)

 [SEE INTERNAL MANAGEMENT SYSTEM, P. 102](#)

Consumer matters

— Consumer satisfaction

 [SEE INTERNAL MANAGEMENT SYSTEM, P. 102](#)

 [SEE MANAGEMENT ASSESSMENT OF PERFORMANCE, RISKS AND OPPORTUNITIES, AND OUTLOOK, P. 146](#)

Human Rights

— Fair labor conditions

 [SEE SUSTAINABILITY, P. 88](#)

— Fair labor conditions (supply chain)

 [SEE SUSTAINABILITY, P. 88](#)

— Supplier relationships

 [SEE GLOBAL OPERATIONS, P. 74](#)

Anti-bribery and corruption

— Ethical business practices

 [SEE RISK AND OPPORTUNITY REPORT, P. 131](#)



GROUP MANAGEMENT REPORT

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Group Management Report: This report contains the Group Management Report of the adidas Group, comprising adidas AG and its consolidated subsidiaries, and the Management Report of adidas AG.

INTERNAL MANAGEMENT SYSTEM

We are committed to increasing shareholder value. We strive to create value by converting sales and operating profit growth into strong operating cash flow, while at the same time managing our asset base proactively. Our company's planning and controlling system is therefore designed to provide a variety of tools to assess our current performance and to align future strategic and investment decisions to best utilize commercial and organizational opportunities in the interest of our shareholders.

INTERNAL MANAGEMENT SYSTEM DESIGNED TO DRIVE SHAREHOLDER VALUE

In order to drive and steer creation of shareholder value, the company's Management focuses on a set of major financial Key Performance Indicators (KPIs). [SEE DIAGRAM 44](#) Sales and operating profit growth, paired with a focus on management of operating working capital, are the main contributors to *operating cash flow* [SEE GLOSSARY](#) improvements. At the same time, value-enhancing capital expenditure benefits future operating profit and cash flow development. In addition, the development of the company's net income position, as well as earnings per share (EPS), is of high importance as it directly drives returns in the interest of our shareholders. [SEE DIAGRAM 44](#) Our strong focus on shareholder value creation is reflected in the fact that our Management's variable compensation is closely linked to the company's growth in sales, profitability and net income. [SEE COMPENSATION REPORT, P. 39](#)

OPERATING MARGIN AS MAJOR KPI FOR OPERATIONAL PROGRESS

Operating margin (defined as operating profit as a percentage of net sales) is one of our company's major KPIs to drive and improve our operational performance. It highlights the quality

of our top line and operational efficiency. The primary drivers to enhance operating margin are as follows:

- **Sales and gross margin development:** Management focuses on identifying and exploiting growth opportunities that not only provide for future top-line improvements, but also have potential to increase our gross margin. Major levers for enhancing our sales and gross margin include:
 - Minimizing clearance activities, while at the same time increasing the full-price share of sales.
 - Optimizing our product mix.
 - Improving the quality of distribution, with a particular focus on e-commerce and *controlled space* [SEE GLOSSARY](#).
 - Realizing supply chain efficiency initiatives.
- **Operating expense control:** Management puts high emphasis on tightly controlling operating expenses to leverage sales growth through to the bottom line. This requires a particular focus on ensuring flexibility in the company's cost base. *Marketing expenditure* [SEE GLOSSARY](#) is one of our largest operating expenses and at the same time one of the most important mechanisms for driving brand desirability and top-line growth sustainably.

Therefore, we are committed to improving the efficiency of our marketing investments. This includes concentrating our communication efforts on key global brand initiatives and focusing our promotion spend on well-selected partnerships with top events, leagues, clubs, federations, athletes and artists. We also aim to increase operational efficiency by tightly managing *operating overhead expenses* [SEE GLOSSARY](#). In this respect, we regularly review our operational structure – harmonizing business processes, standardizing systems, eliminating redundancies and leveraging the scale of our organization.

TIGHT OPERATING WORKING CAPITAL MANAGEMENT

Due to a comparatively low level of fixed assets required in our business, the efficiency of the balance sheet depends to a large degree on our operating working capital management. In this context, our key metric is average operating working capital as a percentage of net sales. Monitoring the development of this metric facilitates the measurement of our progress in improving the efficiency of our business cycle.

Major Key Performance Indicators (KPIs)

44



We strive to proactively manage our inventory levels to meet market demand and ensure fast replenishment. Inventory aging is controlled carefully to reduce inventory obsolescence and to minimize clearance activities. As a result, Inventory Days Lasting (IDL) is monitored and assessed regularly as it measures the average number of days goods remain in inventory before being sold, highlighting the efficiency of capital locked up in products. To optimize capital tied up in accounts receivable, we strive to improve collection efforts in order to reduce the Days of Sales Outstanding (DSO) and improve the aging of accounts receivable. Likewise, we strive to optimize payment terms with our suppliers to best manage our accounts payable.

CAPITAL EXPENDITURE TARGETED TO MAXIMIZE FUTURE RETURNS

Improving the effectiveness of *capital expenditure* [SEE GLOSSARY](#) is another major lever to maximize our operating cash flow. We control capital expenditure with a *top-down, bottom-up* approach. [SEE GLOSSARY](#) In a first step, Management defines focus areas within the framework of our strategic business plan 'Creating the New' and an overall investment budget based on investment requests from various functions within the organization. Then, in a second step, our operating segments align their initiatives within the scope of assigned priorities and available budget. We evaluate potential return on planned investments utilizing the net present value method. Risk is accounted for, adding a risk premium to the cost of capital and thus reducing our estimated future earnings streams where appropriate. By means of scenario planning, the sensitivity of investment returns is tested against changes in initial assumptions. For large investment projects, timelines and deviations versus budget are monitored on a monthly basis throughout the course of the project.

In addition to optimizing return on investments, we evaluate larger projects upon completion and document learnings for future capital expenditure decisions.

NET INCOME AND EARNINGS PER SHARE TO FOCUS ON SHAREHOLDER INTERESTS

Beyond our ambition to maximize operating cash flow, we are committed to a continuous improvement in the company's bottom line. We are convinced that, by doing so, we place an even stronger focus on the interests of our shareholders. Consequently, Management closely monitors the development of both net income and earnings per share (EPS) and executes against these two major financial KPIs. [SEE DIAGRAM 44](#) Our strong focus on driving sustainable expansion to the company's bottom line is also reflected in the fact that, as part of the new Long-Term Incentive Plan 2018/2020, the variable compensation for our Management is directly linked to the company's net income growth.

[SEE COMPENSATION REPORT, P. 39](#)

NON-FINANCIAL KEY PERFORMANCE INDICATORS

In addition to the major financial KPIs to assess the performance and operational success of our company, as outlined above, we have identified a set of non-financial KPIs that help us track our progress in areas that are critical for our long-term success but are not directly reflected in the financial statements. These non-financial KPIs are assessed on a regular basis and managed by the respective business functions. Non-financial KPIs which we are closely monitoring include, amongst others, *Net Promoter Score (NPS)* [SEE GLOSSARY](#), market share, backlogs and sell-through data as well as our customer delivery performance (On-Time In-Full), employee engagement and a set of KPIs in the area of our sustainability performance.

Net Promoter Score (NPS): [F](#) Maintaining and enhancing brand desirability through the creation of strong brand identities is crucial for sustaining and driving profitable growth. Therefore, mainly on a market and category level, we invest in primary qualitative and quantitative research such as trend scouting and consumer surveys to determine brand loyalty and brand strength. Measures that are tracked include brand awareness, likeability and purchase intent.

Furthermore, within the framework of Creating the New, we implemented an NPS system, which strengthens our capabilities to more carefully review brand advocacy as NPS tells us how likely it is that consumers will recommend our brands. NPS is a key pillar in transforming our company into a consumer-centric organization. It represents a holistic and transparent measure of brand performance and has been successfully applied in other industries and organizations. NPS comes from the following question asked to a surveyed group of people: 'How likely is it that you would recommend this brand to a friend?' The answer has a scale from 0 to 10 with 10 being the most likely. NPS is calculated using Promoters (consumers that answered 9 or 10) minus Detractors (consumers that answered 0 to 6). Consumers answering 7 or 8 are called Neutrals or Passives and are not taken into consideration for the calculation of the NPS.

Our efforts around NPS (both our own NPS as well as the NPS of our major competitors) are driven by an independent agency and monitored by our internal global consumer insight teams on a regular basis. In addition, NPS is measured across many of our own-retail stores as well as our own e-commerce platform. We firmly believe that advocacy will create sustained growth for our brands, underpinned by the fact that brand advocates on average buy more than non-advocates. In addition, a large part of our consumers rely on referrals by friends or family when making purchase decisions. [J](#)

Market share: To measure the operational performance of our brands relative to our major competitors, we continuously collect, on a market and category level, market share data. [SEE CORPORATE STRATEGY, P. 62](#) The findings provide detailed insights for our senior management team into which markets and categories we have been able to gain market share relative to our peers, enabling us to leverage those insights across the organization. [SEE MANAGEMENT ASSESSMENT OF PERFORMANCE, RISKS AND OPPORTUNITIES, AND OUTLOOK, P. 146](#) In addition, the results help us to define clear roles and responsibilities for each of our markets and categories within our long-term strategic aspirations, based on their overall positioning within the sporting goods industry.

Backlogs and sell-through data: To manage demand planning and better anticipate our future performance, *backlogs* [SEE GLOSSARY](#) comprising orders received up to nine months in advance of the actual sale are monitored closely. However, due to the growing share of own retail (including our own e-commerce channel) in our business mix, fluctuating order patterns among our customers as well as an increasing part of our business being realized under significantly shortened lead times, orders received from our retail partners are less indicative of anticipated revenues for adidas compared to the past. Therefore, qualitative feedback from our retail partners on the sell-through success of our products at the point of sale as well as such data received from our own-retail activities is becoming increasingly important.

On-Time In-Full (OTIF): OTIF measures the company's delivery performance towards customers and our own-retail stores. Managed by our Global Operations function, OTIF assesses to what degree customers received what they ordered and if they received it on time. [SEE GLOBAL OPERATIONS, P. 74](#) It helps us to investigate improvement potential in the area of order book management and logistics processes. It

therefore also helps us to improve our delivery performance, which is a major aspect when it comes to customer satisfaction. The OTIF assessment covers both the adidas and Reebok brands in most of our key markets. [SEE MANAGEMENT ASSESSMENT OF PERFORMANCE, RISKS AND OPPORTUNITIES, AND OUTLOOK, P. 146](#)

Employee engagement: To measure the level of engagement and motivation of our employees, adidas carries out employee engagement surveys. These surveys aim to provide key insights into how well we, as an employer, are doing in engaging our employees. They thus enable us to develop the right focus and future people strategies across our organization, helping us to create a world-class employee experience and continue to attract and retain top talent. Against the background of organizational and management changes within the company, a new approach and system platform for measuring the level of employee engagement was implemented in 2017.

[SEE PEOPLE AND CULTURE, P. 81](#)

Sustainability performance: We have a strong commitment to enhance the social and environmental performance of our company. By doing so, we firmly believe we will not only improve the company's overall reputation, but also increase its economic value. We therefore follow a comprehensive roadmap with clear targets and regularly track our progress toward these targets. [SEE MANAGEMENT ASSESSMENT OF PERFORMANCE, RISKS AND OPPORTUNITIES, AND OUTLOOK, P. 146](#) A major focus lies on measuring the environmental footprint of our own sites globally as well as monitoring and rating our supplier factories with regard to social and environmental compliance with our Workplace Standards. [SEE SUSTAINABILITY, P. 88](#) We have a strong track record in sustainability disclosure, providing regular updates about our sustainability performance in the company's Annual Report as well as on our corporate website. [➔ ADIDAS-GROUP.COM/S/SUSTAINABILITY-REPORTS](https://www.adidas-group.com/s/sustainability-reports)

STRUCTURED PERFORMANCE MEASUREMENT SYSTEM

We have developed an extensive performance measurement system, which utilizes a variety of tools to measure the company's performance. Key performance indicators as well as other important financial metrics are monitored and compared against initial targets as well as *rolling forecasts* [SEE GLOSSARY](#) on a monthly basis. When negative deviations exist between actual and target numbers, we perform a detailed analysis to identify and address the cause. If necessary, action plans are implemented to optimize the development of our operating performance. To assess current sales and profitability development, Management continuously analyzes the performance of our operating segments. We also benchmark our financial results with those of our major competitors on a regular basis.

Taking into account year-to-date performance as well as opportunities and risks, the company's full year financial performance is assessed on a monthly basis. In this respect, also backlogs, sell-through data, feedback from customers and own-retail stores are assessed as available. Finally, as a further early indicator for future performance, the results of any relevant recent market and consumer research are assessed as available.

BUSINESS PERFORMANCE

In 2017, adidas recorded strong operational and financial improvements. Revenues increased 16% on a currency-neutral basis, driven by strong double-digit growth at the adidas brand and a mid-single-digit sales increase at Reebok. All market segments recorded double-digit currency-neutral sales increases, with the exception of Russia/CIS, where revenues declined. The gross margin increased 1.2 percentage points to 50.4%, mainly reflecting an improved pricing and product mix. Other operating expenses as a percentage of sales were down 0.8 percentage points to 41.9%. Despite the non-recurrence of a one-time gain related to the early termination of the Chelsea F.C. sponsorship that was included in the prior year, the company's operating margin increased 1.2 percentage points to 9.8%. As a result of a revaluation of the company's US deferred tax assets, which became necessary following the implementation of the US tax reform, the company recorded a negative one-time tax impact in the amount of € 76 million in 2017. Excluding this negative one-time tax impact, net income from continuing operations increased 32% to € 1.430 billion. This translates into basic EPS from continuing operations of € 7.05, representing an increase of 31% versus the prior year period.

ECONOMIC AND SECTOR DEVELOPMENT

GLOBAL ECONOMY ACCELERATES IN 2017¹

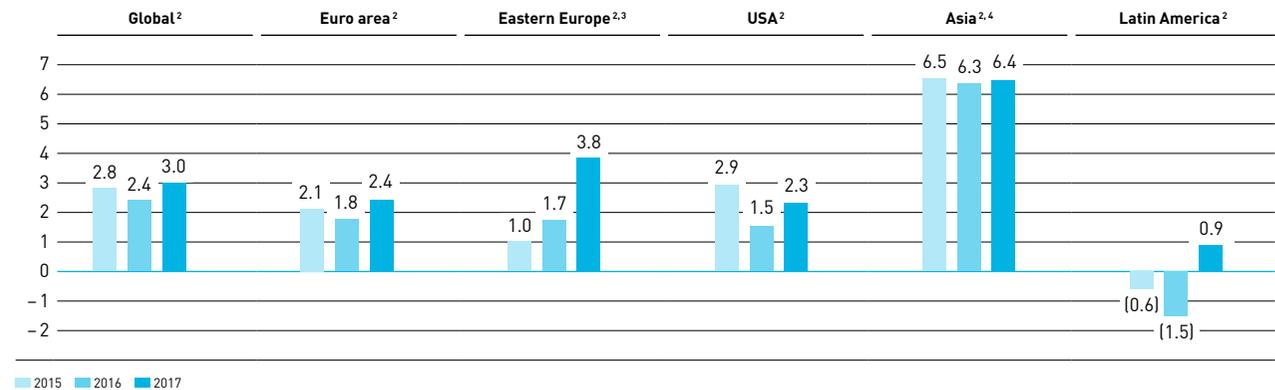
The global economy gained pace during 2017, with global gross domestic product (GDP) expanding 3.0%. The upswing was driven by a rise in consumer confidence, a pick-up in manufacturing activity, a stabilization of commodity prices

and benign financing conditions. Moreover, a simultaneous recovery in major developed economies as well as developing economies provided a major boost to global trade. Despite domestic policy uncertainty in major economies, developed

economies grew 2.3% in 2017, supported by improving labor market conditions as well as accommodative monetary policies. In particular, topics around international relations, such as the ongoing Brexit negotiations, remained a political

Regional GDP development¹ in %

45



1 Real change in percent versus prior year; 2015 and 2016 figures restated compared to prior year.
2 Source: World Bank.
3 Includes Emerging Europe and Central Asia.
4 Includes East Asia and Pacific.

Quarterly unemployment rate by region¹ in % of total active population

46

	Q4 2016	Q1 2017	Q2 2017	Q3 2017	Q4 2017
USA ²	4.7	4.5	4.3	4.2	4.1
Euro area ³	9.6	9.4	9.1	8.9	8.7
Japan ⁴	3.1	2.8	2.8	2.8	2.7
China ⁵	4.0	4.0	4.0	4.0	4.0
Russia ⁶	5.3	5.4	5.1	5.1	5.1
Brazil ⁷	11.9	13.7	13.0	12.4	12.0

1 Quarter-end figures except for Q4 figures (refer to November data).
2 Source: US Bureau of Labor Statistics.
3 Source: Eurostat.
4 Source: Japan Ministry of Internal Affairs and Communications.
5 Source: China Ministry of Human Resources and Social Security.
6 Source: Russia Federal Service of State Statistics.
7 Source: Brazil Institute of Geography and Statistics.

Quarterly development of consumer price index¹ by region

47

	Q4 2016	Q1 2017	Q2 2017	Q3 2017	Q4 2017
USA ²	2.1	2.4	1.6	2.2	2.2
Euro area ³	1.1	1.5	1.3	1.5	1.4
Japan ⁴	0.3	0.2	0.4	0.7	0.6
China ⁵	2.1	0.9	1.5	1.6	1.8
Russia ⁶	5.4	4.3	4.4	3.0	2.5
Brazil ⁷	6.3	4.6	3.0	2.5	3.0

1 Quarter-end figures except for Q4 figures (refer to November data).
2 Source: US Bureau of Labor Statistics.
3 Source: Eurostat.
4 Source: Japan Ministry of Internal Affairs and Communications.
5 Source: China National Bureau of Statistics.
6 Source: Russia Federal Service of State Statistics.
7 Source: Brazil Institute of Geography and Statistics.

1 Source: World Bank Global Economic Prospects.

overhang but were less of a drag on economic activity than previously expected. At 4.3%, growth in developing economies accelerated, as obstacles to economic activity diminished in commodity-exporting countries and commodity prices experienced a further stabilization.

ROBUST GROWTH IN THE SPORTING GOODS INDUSTRY CONTINUES

The global sporting goods industry continued to grow at robust rates in 2017, despite a moderate deceleration of momentum in individual regions. In particular, sector growth in North America was slower than in previous years as the marketplace was negatively impacted by a further consolidation in US retail and by supply-demand mismatches in certain categories. Most other markets expanded, driven by global trends such as increasing penetration of sportswear ('athleisure') ■ SEE GLOSSARY, rising sports participation rates and increasing health awareness. Moreover, digital developments continued to reshape the sports industry around the world. Social fitness remained an overriding theme and the e-commerce channel continued to see rapid

expansion, as retailers are leveraging both mobile technologies and social media tools. From a category perspective, athletic footwear continued to drive the sector in 2017, supported by ongoing high demand for various casual and running styles. Basketball footwear, on the other hand, remained challenged throughout the year. Growth in the overall athletic apparel category was more muted in the absence of major global sports events during 2017. Nevertheless, underlying demand for activewear apparel remained robust, as consumers continued to reallocate wallet share away from traditional apparel. The equipment category recorded another mixed year in 2017, albeit with signs of stabilization in some areas.

Exchange rate development¹ € 1 equals 49

	Average rate 2016	Q1 2017	Q2 2017	Q3 2017	Q4 2017	Average rate 2017
USD	1.1069	1.0691	1.1412	1.1806	1.1993	1.1266
GBP	0.8188	0.8555	0.8793	0.8818	0.8872	0.8754
JPY	120.40	119.55	127.75	132.82	135.01	126.24
RUB	74.278	60.274	67.428	68.495	69.080	65.560
CNY	7.3515	7.3760	7.8664	7.8355	7.8365	7.6116

¹ Spot rates at quarter-end.

Quarterly consumer confidence development¹ by region 48

	Q4 2016	Q1 2017	Q2 2017	Q3 2017	Q4 2017
USA ²	113.3	124.9	117.3	120.6	123.1
Euro area ³	(5.1)	(5.1)	(1.3)	(1.2)	0.5
Japan ⁴	42.3	43.9	43.3	43.9	44.7
China ⁵	108.4	111.0	113.3	118.6	122.6
Russia ⁶	(18.0)	(15.0)	(14.0)	(11.0)	(11.0)
Brazil ⁷	100.3	102.0	100.5	98.5	100.5

¹ Quarter-end figures.

² Source: Conference Board.

³ Source: European Commission.

⁴ Source: Economic and Social Research Institute, Government of Japan.

⁵ Source: China National Bureau of Statistics.

⁶ Source: Russia Federal Service of State Statistics.

⁷ Source: Brazil National Confederation of Industry.

INCOME STATEMENT

ADIDAS DELIVERS STRONG FINANCIAL PERFORMANCE IN 2017

In 2017, revenues increased 16% on a currency-neutral basis. In euro terms, revenues grew 15% to € 21.218 billion from € 18.483 billion in 2016. [SEE DIAGRAM 50](#) From a market segment perspective, currency-neutral sales grew at double-digit rates in all regions in 2017, except for Russia/CIS, where revenues declined. [SEE BUSINESS PERFORMANCE BY SEGMENT, P. 124](#)

Net sales^{1,2} € in millions

50

2017	21,218
2016	18,483
2015	16,915
2014	14,534
2013	14,203

¹ 2017 and 2016 figures reflect continuing operations as a result of the divestiture of the Rockport, TaylorMade, Adams Golf, Ashworth and CCM Hockey businesses.

² 2015, 2014 and 2013 figures reflect continuing operations as a result of the divestiture of the Rockport business.

Net sales by segment € in millions

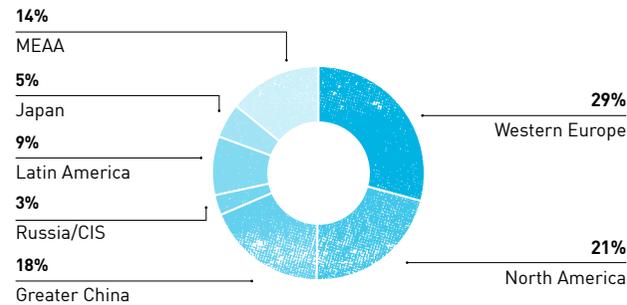
51

	2017	2016	Change	Change (currency-neutral)
Western Europe	5,883	5,291	11%	13%
North America	4,275	3,412	25%	27%
Greater China	3,789	3,010	26%	29%
Russia/CIS	660	679	[3%]	[13%]
Latin America	1,907	1,731	10%	12%
Japan	1,056	1,007	5%	10%
MEAA	2,907	2,685	8%	10%
Other Businesses ¹	739	667	11%	12%
Total	21,218	18,483	15%	16%

¹ Figures reflect continuing operations as a result of the divestiture of the Rockport, TaylorMade, Adams Golf, Ashworth and CCM Hockey businesses.

Net sales by region¹ in % of net sales

52



¹ Figures reflect all operating activities of the operating segments, including Other Businesses.

ADIDAS BRAND REVENUES GROW AT STRONG DOUBLE-DIGIT RATE

Currency-neutral revenues for the adidas brand increased 18%, driven by double-digit sales increases in the running and outdoor categories as well as at adidas Originals and adidas neo. In addition, high-single-digit sales increases in the training category also contributed to this development. In euro terms, adidas brand revenues grew 16% to € 18.993 billion compared to € 16.334 billion in 2016. Currency-neutral Reebok brand sales were up 4% versus the prior year, driven by double-digit sales increases in Classics as well as low-single-digit growth in the running category. While Reebok's international revenues grew at a double-digit rate in 2017, sales in the US declined, reflecting the significant amount of store closures in the market. In euro terms, Reebok sales increased 4% to € 1.843 billion (2016: € 1.770 billion).

SALES GROW IN FOOTWEAR AND APPAREL

Currency-neutral footwear sales grew 24% in 2017, driven by double-digit growth in the running category as well as at adidas Originals and adidas neo. In addition, high-single-digit increases in the football and training categories also contributed to this development. Apparel revenues grew 7% on a currency-neutral basis, due to double-digit increases in the outdoor category as well as at adidas Originals. In addition, high-single-digit growth in the training category also contributed to this development. Currency-neutral accessory and hardware sales were up 6%, driven by double-digit growth at adidas Originals and adidas neo. [SEE DIAGRAM 53](#)

Net sales by product category¹ € in millions

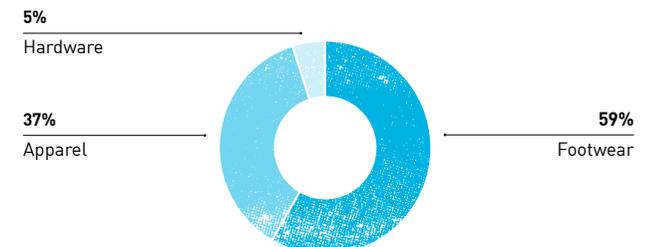
53

	2017	2016	Change	Change (currency-neutral)
Footwear	12,427	10,132	23%	24%
Apparel	7,747	7,352	5%	7%
Hardware	1,044	999	5%	6%
Total	21,218	18,483	15%	16%

¹ Figures reflect continuing operations as a result of the divestiture of the Rockport, TaylorMade, Adams Golf, Ashworth and CCM Hockey businesses.

Net sales by product category¹ in % of net sales

54



¹ Figures reflect continuing operations as a result of the divestiture of the Rockport, TaylorMade, Adams Golf, Ashworth and CCM Hockey businesses.

COST OF SALES INCREASES

Cost of sales is defined as the amount we pay to third parties for expenses associated with producing and delivering our products. In addition, own-production expenses are also included in the cost of sales. However, these expenses represent only a very small portion of total cost of sales. In 2017, cost of sales was € 10.514 billion, representing an increase of 12% compared to the prior year level of € 9.383 billion. This development reflects the strong growth of our business as well as less favorable hedging rates and higher input costs mainly due to an increase in material and labor costs.

GROSS MARGIN IMPROVES 1.2 PERCENTAGE POINTS

In 2017, the gross profit increased 18% to € 10.703 billion from € 9.100 billion in 2016, representing a gross margin increase of 1.2 percentage points to 50.4% [2016: 49.2%]. [SEE DIAGRAM 55](#) This development was due to the positive effects from a better pricing and product mix, which more than offset negative currency effects as well as higher input costs.

Gross margin^{1,2,3} in % 55

Year	Gross margin (%)
2017	50.4
2016	49.2
2015	48.3
2014	47.6
2013	49.3

¹ Gross margin = (gross profit / net sales) × 100.

² 2017 and 2016 figures reflect continuing operations as a result of the divestiture of the Rockport, TaylorMade, Adams Golf, Ashworth and CCM Hockey businesses.

³ 2015, 2014 and 2013 figures reflect continuing operations as a result of the divestiture of the Rockport business.

ROYALTY AND COMMISSION INCOME INCREASES

Royalty and commission income increased 11% on a currency-neutral basis and 10% in euro terms to € 115 million [2016: € 105 million].

OTHER OPERATING INCOME DECLINES

In 2017, other operating income declined 49% to € 133 million from € 262 million in 2016. This development mainly reflects the non-recurrence of two one-time gains in 2016, which were related to the early termination of the Chelsea F.C. contract as well as the divestiture of the Mitchell & Ness business.

OTHER OPERATING EXPENSES AS A PERCENTAGE OF SALES DOWN 0.8 PERCENTAGE POINTS

Other operating expenses, including depreciation and amortization, consist of marketing expenditure as well as operating overhead costs. In 2017, other operating expenses were up 13% to € 8.882 billion [2016: € 7.885 billion], reflecting an increase in marketing expenditure as well as higher operating overhead expenditure. [SEE NOTE 32, P. 201](#) As a percentage of sales, other operating expenses decreased 0.8 percentage points to 41.9% from 42.7% in 2016. [SEE DIAGRAM 56](#) Marketing expenditure amounted to € 2.732 billion in 2017 compared to € 2.410 billion in the prior year, representing an increase of 13% compared to the 2016 level. As a percentage of sales, marketing expenditure declined 0.2 percentage points to 12.9% [2016: 13.0%], reflecting the company's strong top-line development. [SEE DIAGRAM 57](#) Operating overhead expenses increased 12% to € 6.150 billion in 2017 from € 5.475 billion in the prior year. As a percentage of sales, operating overhead expenses declined 0.6 percentage points to 29.0% from 29.6% in the prior year, reflecting the company's focus on executing the strategic business plan 'Creating the New' as well as the strong operational performance in 2017.

Other operating expenses^{1,2} in % of net sales 56

Year	Other operating expenses (%)
2017	41.9
2016	42.7
2015	43.1
2014	42.7
2013	42.3

¹ 2017 and 2016 figures reflect continuing operations as a result of the divestiture of the Rockport, TaylorMade, Adams Golf, Ashworth and CCM Hockey businesses.

² 2015, 2014 and 2013 figures reflect continuing operations as a result of the divestiture of the Rockport business.

Marketing expenses^{1,2} in % of net sales 57

Year	Marketing expenses (%)
2017	12.9
2016	13.0
2015	13.9
2014	13.2
2013	12.6

¹ 2017 and 2016 figures reflect continuing operations as a result of the divestiture of the Rockport, TaylorMade, Adams Golf, Ashworth and CCM Hockey businesses.

² 2015, 2014 and 2013 figures reflect continuing operations as a result of the divestiture of the Rockport business.

EBITDA INCREASES 29%

Earnings before interest, taxes, depreciation and amortization as well as impairment losses/reversal of impairment losses on property, plant and equipment and intangible assets (EBITDA) increased 29% to € 2.511 billion in 2017 versus € 1.953 billion in 2016. [SEE DIAGRAM 58](#) Depreciation and amortization expense for tangible and intangible assets (excluding impairment losses/reversal of impairment losses) increased 23% to € 452 million in 2017 (2016: € 368 million). This development is mainly due to an increase in property, plant and equipment. In accordance with IFRS, intangible assets with indefinite useful lives (*goodwill* [SEE GLOSSARY](#) and trademarks) are tested annually and additionally when there are indications of potential impairment. In this connection, an impairment of intangible assets with unlimited useful lives was incurred in 2017.

EBITDA^{1,2,3} € in millions **58**

2017	2,511
2016	1,953
2015	1,475
2014	1,283
2013	1,496

1 EBITDA = Income before taxes (IBT) + net interest expenses + depreciation and amortization.
2 2017 and 2016 figures reflect continuing operations as a result of the divestiture of the Rockport, TaylorMade, Adams Golf, Ashworth and CCM Hockey businesses.
3 2015, 2014 and 2013 figures reflect continuing operations as a result of the divestiture of the Rockport business.

**OPERATING MARGIN INCREASES
1.2 PERCENTAGE POINTS**

Operating profit grew 31% to € 2.070 billion in 2017 versus € 1.582 billion in 2016. [SEE DIAGRAM 59](#) This represents an operating margin increase of 1.2 percentage points to 9.8% compared to the prior year level of 8.6%. [SEE DIAGRAM 60](#) This development was due to the gross margin increase as well as

Operating profit^{1,2,3,4,5} € in millions **59**

2017	2,070
2016	1,582
2015	1,094
2014	961
2013	1,233

1 2017 and 2016 figures reflect continuing operations as a result of the divestiture of the Rockport, TaylorMade, Adams Golf, Ashworth and CCM Hockey businesses.
2 2015, 2014 and 2013 figures reflect continuing operations as a result of the divestiture of the Rockport business.
3 2015 excluding goodwill impairment of € 34 million.
4 2014 excluding goodwill impairment of € 78 million.
5 2013 excluding goodwill impairment of € 52 million.

Operating margin^{1,2,3,4,5,6} in % **60**

2017	9.8
2016	8.6
2015	6.5
2014	6.6
2013	8.7

1 Operating margin = (operating profit / net sales) × 100.
2 2017 and 2016 figures reflect continuing operations as a result of the divestiture of the Rockport, TaylorMade, Adams Golf, Ashworth and CCM Hockey businesses.
3 2015, 2014 and 2013 figures reflect continuing operations as a result of the divestiture of the Rockport business.
4 2015 excluding goodwill impairment of € 34 million.
5 2014 excluding goodwill impairment of € 78 million.
6 2013 excluding goodwill impairment of € 52 million.

Net financial expenses € in millions **61**

2017	47
2016	46
2015	21
2014	48
2013	68

the positive effect from lower other operating expenses as a percentage of sales, partly offset by the decline in other operating income.

NET FINANCIAL EXPENSES INCREASE

Financial income increased 68% to € 46 million in 2017 (2016: € 28 million), mainly due to positive exchange rate effects. Financial expenses were up 26% to € 93 million compared to € 74 million in 2016. This development was due to an increase in other financial expenses as a result of impairment losses on other financial assets. As a result, the company recorded net financial expenses of € 47 million, an increase of 1% compared to the prior year level of € 46 million. [SEE DIAGRAM 61](#)

**TAX RATE INCREASES 3.5 PERCENTAGE
POINTS TO 33.0%**

The company's tax rate in 2017 reached a level of 33.0%, representing an increase of 3.5 percentage points compared to the prior year level of 29.6%. This development was solely driven by a negative one-time tax impact in the amount of € 76 million, reflecting a revaluation of the company's US deferred tax assets, which became necessary following the implementation of the US tax reform. Excluding this negative, non-cash-relevant tax impact, the company's tax rate decreased 0.3 percentage points to 29.3%.

**NET INCOME FROM CONTINUING OPERATIONS
EXCLUDING ONE-TIME TAX IMPACT UP 32%
TO € 1.430 BILLION**

Excluding the negative one-time tax impact, net income from continuing operations increased 32% to € 1.430 billion versus € 1.082 billion in 2016. [SEE DIAGRAM 62](#) Basic EPS from continuing operations increased 31% to € 7.05 from € 5.39 in 2016. [SEE DIAGRAM 63](#) Diluted EPS from continuing operations was up 32% to € 7.00 in 2017 (2016: € 5.29).

Including the one-time tax impact, net income from continuing operations rose 25% to € 1.354 billion (2016: € 1.082 billion). Basic EPS from continuing operations increased 24% from € 5.39 in 2016 to € 6.68 in 2017. Diluted EPS from continuing operations was up 25% to € 6.63 in 2017 (2016: € 5.29).

The total number of shares outstanding increased by 2,371,924 shares in 2017 to 203,861,234 as a result of share conversions in relation to the company's outstanding convertible bond which were partly offset by shares repurchased as part of the company's share buyback program. [SEE FINANCIAL HIGHLIGHTS, P. 4](#) Consequently, the average number of shares used in the calculation of basic earnings per share (EPS) was 202,391,673 (2016: 200,188,276).

LOSSES FROM DISCONTINUED OPERATIONS AMOUNT TO € 254 MILLION

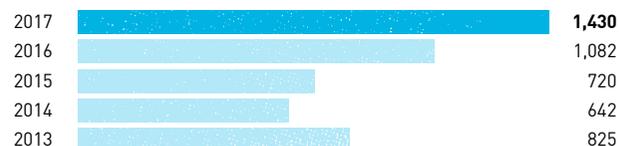
In 2017, adidas incurred losses from discontinued operations of € 254 million, net of tax, mainly related to the TaylorMade and CCM Hockey businesses (2016: losses of € 62 million). These losses from discontinued operations were due to a loss recognized on the measurement to fair value less costs to sell, net of tax, in the amount of € 256 million, partly offset by income from discontinued operating activities of € 1 million.

NET INCOME ATTRIBUTABLE TO SHAREHOLDERS EXCLUDING ONE-TIME TAX IMPACT INCREASES 15% TO € 1.173 BILLION

The company's net income attributable to shareholders, which in addition to net income from continuing operations includes the losses from discontinued operations, grew 15% to € 1.173 billion (2016: € 1.017 billion) excluding the negative one-time tax impact. As a result, basic EPS from continuing and discontinued operations increased 14% to € 5.79 versus € 5.08 in 2016, while diluted EPS from continuing and discontinued operations grew 15% to € 5.75 (2016: € 4.99).

Including the negative one-time tax impact, the company's net income attributable to shareholders increased 8% to € 1.097 billion (2016: € 1.017 billion). Basic EPS from continuing and discontinued operations increased 7% to € 5.42 (2016: € 5.08) and diluted EPS from continuing and discontinued operations grew 8% to € 5.38 (2016: € 4.99).

Net income from continuing operations^{1,2,3,4} **62**
€ in millions



1 2017 excluding negative one-time tax impact of € 76 million.

2 2015 excluding goodwill impairment of € 34 million.

3 2014 excluding goodwill impairment of € 78 million.

4 2013 excluding goodwill impairment of € 52 million.

Basic earnings per share^{1,2,3,4,5} in € **63**



1 Figures reflect continuing operations.

2 2017 excluding negative one-time tax impact of € 76 million.

3 2015 excluding goodwill impairment of € 34 million.

4 2014 excluding goodwill impairment of € 78 million.

5 2013 excluding goodwill impairment of € 52 million.

STATEMENT OF FINANCIAL POSITION AND STATEMENT OF CASH FLOWS

DIVESTITURE OF THE TAYLORMADE AND CCM HOCKEY BUSINESSES

On September 1, 2017, we formally completed the divestiture of the CCM Hockey business. In addition, as of October 2, 2017, the TaylorMade business (including the TaylorMade, Adams Golf and Ashworth brands) was divested. As a result, all relevant assets and liabilities were derecognized from the consolidated statement of financial position as of these dates. However, a restatement of the 2016 balance sheet items is not permitted under IFRS. [SEE NOTE 04, P. 169](#)

ASSETS

At the end of December 2017, total assets were down 4% to € 14.522 billion versus € 15.176 billion in the prior year, as a result of a decrease in both current assets as well as non-current assets. [SEE DIAGRAM 64](#)

Structure of statement of financial position¹ in % of total assets 64

	2017	2016
Assets (€ in millions)	14,522	15,176
Cash and cash equivalents	11.0	9.9
Accounts receivable	15.9	14.5
Inventories	25.4	24.8
Fixed assets ²	33.9	35.4
Other assets	13.7	15.4

■ 2017 ■ 2016

¹ For absolute figures see adidas AG Consolidated Statement of Financial Position, p. 119.

² Fixed assets = property, plant and equipment + goodwill + trademarks + other intangible assets + long-term financial assets.

Total current assets decreased 3% to € 8.645 billion at the end of December 2017 compared to € 8.886 billion in 2016. Cash and cash equivalents were up 6% to € 1.598 billion at the end of December 2017 from € 1.510 billion in the prior year, as net cash generated from operating activities was only partly offset by net cash used in investing and financing activities. Currency effects had a negative impact on cash and cash equivalents in an amount of € 111 million. Inventories decreased 2% to € 3.692 billion at the end of December 2017 from € 3.763 billion in 2016. [SEE NOTE 09, P. 170](#) [SEE DIAGRAM 66](#) On a currency-neutral basis, inventories grew 4%. Inventories from continuing operations increased 2% (+8% currency-neutral), reflecting higher stock levels to support the company's top-line momentum. Accounts receivable increased 5% to € 2.315 billion at the end of December 2017 (2016: € 2.200 billion). [SEE NOTE 07, P. 169](#) [SEE DIAGRAM 67](#) On a currency-neutral basis, receivables were up 13%. Receivables from continuing operations increased 15% (+23% currency-neutral), mainly reflecting the company's top-line development in 2017. Other current financial assets declined 46% to € 393 million at the end of December 2017 from € 729 million in 2016. [SEE NOTE 08, P. 170](#) This development was mainly due to

Structure of statement of financial position¹ in % of total liabilities and equity 65

	2017	2016
Liabilities and equity (€ in millions)	14,522	15,176
Short-term borrowings	0.9	4.2
Accounts payable	13.6	16.4
Long-term borrowings	6.8	6.5
Other liabilities	34.4	30.4
Total equity	44.3	42.5

■ 2017 ■ 2016

¹ For absolute figures see adidas AG Consolidated Statement of Financial Position, p. 119.

a decrease in the fair value of financial instruments as well as a decrease in other financial assets, which was mainly related to the non-recurrence of the extraordinary receivable related to the early termination of the Chelsea F.C. contract. Other current assets were down 14% to € 498 million at the end of December 2017 (2016: € 580 million), mainly due to a decrease in prepaid promotion contracts as well as tax receivables other than income taxes. [SEE NOTE 10, P. 170](#) Assets

Inventories € in millions 66

2017	3,692
2016	3,763
2015	3,113
2014	2,526
2013	2,634

Accounts receivable € in millions 67

2017	2,315
2016	2,200
2015	2,049
2014	1,946
2013	1,809

Accounts payable € in millions 68

2017	1,975
2016	2,496
2015	2,024
2014	1,652
2013	1,825

classified as held for sale amounted to € 72 million in 2017 due to the concrete plan to sell the Reebok headquarters in Canton. [SEE NOTE 11, P. 170](#)

Total non-current assets declined 7% to € 5.877 billion at the end of December 2017 from € 6.290 billion in 2016. Fixed assets decreased 8% to € 4.920 billion at the end of December 2017 versus € 5.367 billion in 2016. Additions of € 861 million, primarily related to own-retail activities, investments into the company's logistics and IT infrastructure as well as the further development of the company's headquarters in Herzogenaurach, were more than offset by the pre-divestiture reclassification of the net book value of fixed assets of the TaylorMade and CCM Hockey businesses to assets held for sale in an amount of € 392 million. In addition, negative currency effects of € 380 million as well as depreciation and amortization of € 498 million contributed to this development. Other non-current financial assets more than doubled to € 219 million from € 96 million at the end of 2016. [SEE NOTE 16, P. 174](#) This development was mainly due to the recognition of seller and contingent notes related to the divestiture of the TaylorMade and CCM Hockey businesses. Deferred tax assets decreased 14% to € 630 million from € 732 million in 2016 as a result of a revaluation of the company's US deferred tax assets, which became necessary following the implementation of the US tax reform.

LIABILITIES AND EQUITY

Total current liabilities decreased 7% to € 6.291 billion at the end of December 2017 from € 6.765 billion in 2016. Short-term borrowings declined 79% to € 137 million at the end of December 2017 (2016: € 636 million), reflecting conversions of the company's convertible bond into adidas AG shares as well as a decrease in bank loans. Accounts payable were down 21% to € 1.975 billion at the end of December 2017 versus € 2.496 billion in 2016. [SEE DIAGRAM 68](#) On a currency-neutral basis, accounts payable declined 19%. Accounts payable from

continuing operations decreased 17% (–15% currency-neutral), reflecting the company's focus on inventory management as well as improved terms with our suppliers and phasing of sourcing activities. Other current financial liabilities were up 81% to € 362 million from € 201 million in 2016, mainly as a result of an increase in the negative fair value of financial instruments. [SEE NOTE 19, P. 176](#) Other current provisions increased 29% to € 741 million at the end of December 2017 versus € 573 million in 2016, driven by an increase in operational provisions. Current accrued liabilities grew 8% to € 2.180 billion at the end of December 2017 from € 2.023 billion in 2016, mainly as a result of an increase in invoices not yet received as well as higher accruals for customer discounts. Other current liabilities were up 9% to € 473 million at the end of December 2017 from € 434 million in 2016, primarily due to an increase in miscellaneous taxes payable. [SEE NOTE 22, P. 177](#)

Total non-current liabilities decreased 8% to € 1.796 billion at the end of December 2017 from € 1.957 billion in the prior year. Long-term borrowings remained relatively unchanged at € 983 million at the end of December 2017 from € 982 million in the prior year. [SEE NOTE 18, P. 175](#) Deferred tax liabilities decreased 29% to € 275 million from € 387 million in 2016, partly due to the pre-divestiture reclassification of the TaylorMade and CCM Hockey businesses to liabilities held for sale. Other non-current provisions increased 82% to

€ 80 million at the end of December 2017 from € 44 million in the prior year, mainly as a result of an increase in provisions for personnel. Non-current accrued liabilities decreased 29% to € 85 million from € 120 million in 2016 due to a decrease in accruals for personnel as well as invoices not yet received.

[SEE NOTE 21, P. 177](#)

Shareholders' equity decreased to € 6.450 billion at the end of December 2017 versus € 6.472 billion in 2016, driven by negative currency effects of € 525 million as well as the dividend of € 405 million paid to shareholders for the 2016 financial year. In addition, a decrease of hedging reserves of € 375 million as well as the repurchase of treasury shares in an amount of € 89 million, including incidental purchasing costs, also contributed to the decline. These developments more than offset the net income generated during the last twelve months and the reissuance of treasury shares in an amount of € 248 million. The company's equity ratio increased to 44.4% compared to 42.6% in the prior year. [SEE NOTE 26, P. 182](#)

[SEE DIAGRAM 69](#)

OPERATING WORKING CAPITAL

Operating working capital [SEE GLOSSARY](#) increased 16% to € 4.033 billion at the end of December 2017 compared to

Average operating working capital^{1,2,3} in % of net sales **70**

2017	20.4
2016	21.1
2015	20.5
2014	22.4
2013	21.3

¹ Average operating working capital = sum of operating working capital at quarter-end / 4.

Operating working capital = accounts receivable + inventories – accounts payable.

² 2017 and 2016 figures reflect continuing operations as a result of the divestiture of the Rockport, TaylorMade, Adams Golf, Ashworth and CCM Hockey businesses.

³ 2015, 2014 and 2013 figures reflect continuing operations as a result of the divestiture of the Rockport business.

Equity ratio in % **69**

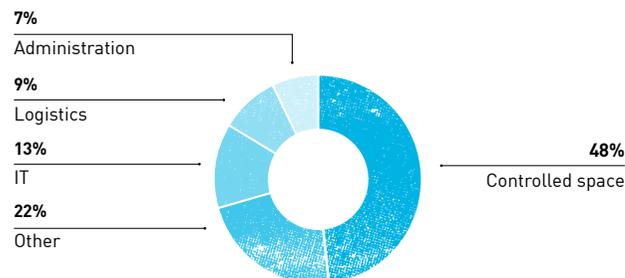
2017	44.4
2016	42.6
2015	42.5
2014	45.3
2013	47.3

€ 3.468 billion in 2016. On a currency-neutral basis, operating working capital grew 27%. Operating working capital from continuing operations rose 25% (+36% currency-neutral). Average operating working capital as a percentage of sales from continuing operations decreased 0.7 percentage points to 20.4% (2016: 21.1%), reflecting the strong top-line development during the last twelve months as well as the company's continued focus on tight working capital management. [SEE DIAGRAM 70](#)

INVESTMENT ANALYSIS

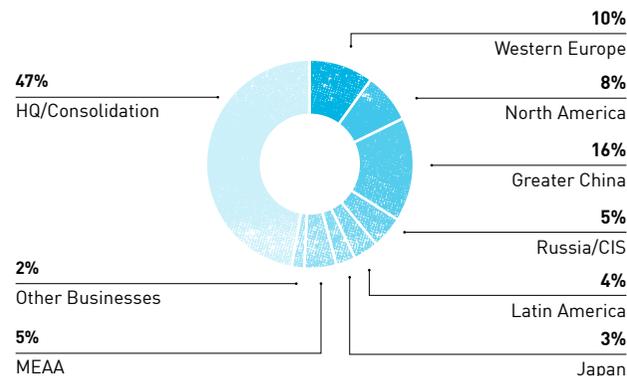
Capital expenditure is defined as the total cash expenditure for the purchase of tangible and intangible assets (excluding acquisitions). Capital expenditure increased 16% to € 755 million in 2017 (2016: € 651 million). Capital expenditure from continuing operations increased 17% to € 752 million from € 642 million in 2016. Capital expenditure for property, plant and equipment was up 16% to € 681 million compared to € 586 million in the prior year. The company invested € 74 million in intangible assets, representing a 14% increase compared to the prior year (2016: € 65 million). Depreciation and amortization excluding impairment losses/reversal of impairment losses of tangible and intangible assets increased 13% to € 421 million in 2017 (2016: € 373 million).

Capital expenditure by type in % of total CAPEX 71



The majority of the company's capital expenditure was related to our controlled space initiatives. Investments in new or remodeled own-retail and franchise stores as well as in shop-in-shop presentations of our brands and products in our customers' stores accounted for 48% of total capital expenditure (2016: 55%). Expenditure for IT and logistics represented 13% and 9%, respectively (2016: 10% and 8%, respectively). In addition, expenditure for administration represented 7% (2016: 9%), while 22% of total capital expenditure was recorded for other initiatives (2016: 18%). [SEE DIAGRAM 71](#) From a regional perspective, the majority of the capital expenditure was recorded at the company's headquarters in Herzogenaurach, Germany, accounting for 47% (2016: 32%). In addition, capital expenditure in Greater China accounted for 16% (2016: 15%) of the total capital expenditure, followed by Western Europe with 10% (2016: 12%), North America with 8% (2016: 13%), MEAA and Russia/CIS with 5% each (2016: 9% and 7%, respectively), Latin America with 4% (2016: 7%) as well as Japan with 3% (2016: 2%). [SEE DIAGRAM 72](#)

Capital expenditure by region in % of total CAPEX 72



LIQUIDITY ANALYSIS

In 2017, net cash generated from operating activities increased to € 1.648 billion (2016: € 1.348 billion). [SEE FINANCIAL HIGHLIGHTS, P. 4](#) Net cash generated from continuing operating activities rose to € 1.641 billion (2016: € 1.309 billion), driven by an increase in income before taxes which was partly offset by higher operating working capital requirements as well as an increase in income taxes paid. Net cash used in investing activities rose to € 680 million (2016: € 614 million). Net cash used in continuing investing activities increased to € 676 million (2016: € 605 million). The majority of continuing investing activities in 2017 related to spending for property, plant and equipment, such as investments in the furnishing and fitting of our own-retail stores and investments in IT systems as well as the purchase of investments and other long-term assets. Net cash used in financing activities and net cash used in continuing financing activities grew to € 769 million each (2016: € 553 million and € 545 million, respectively), mainly due to the dividend paid to shareholders, the repayment of short-term borrowings as well as the repurchase of treasury shares. Exchange rate effects negatively impacted the company's cash position by € 111 million. As a result of all these developments, cash and cash equivalents increased € 88 million to € 1.598 billion at the end of December 2017 compared to € 1.510 billion at the end of December 2016. [SEE DIAGRAM 74](#)

Net borrowings/EBITDA^{1,2} € in millions 73



¹ 2017 and 2016 figures reflect continuing operations as a result of the divestiture of the Rockport, TaylorMade, Adams Golf, Ashworth and CCM Hockey businesses.

² 2015, 2014 and 2013 figures reflect continuing operations as a result of the divestiture of the Rockport business.

Net cash at December 31, 2017 amounted to € 484 million, compared to net borrowings of € 103 million in 2016, representing an improvement of € 587 million compared to the prior year. This development was driven by the increase in cash generated from operating activities as well as proceeds arising from the disposal of the TaylorMade and CCM Hockey businesses, partly offset by the utilization of cash for the purchase of fixed assets as well as the dividend paid to shareholders and the repurchase of adidas AG shares. In addition, the conversion of convertible bonds into adidas AG shares also contributed to this improvement. [SEE TREASURY, P. 115](#) The company's ratio of net borrowings over EBITDA amounted to –0.2 at the end of December 2017 (2016: 0.1), which is within the company's mid-term target corridor of below two times.

[SEE DIAGRAM 73](#)

Operating cash flow, as described in the Internal Management System, increased 24% to € 1.202 billion in 2017 from € 969 million in 2016, mainly due to the higher operating profit.

[SEE INTERNAL MANAGEMENT SYSTEM, P. 102](#)

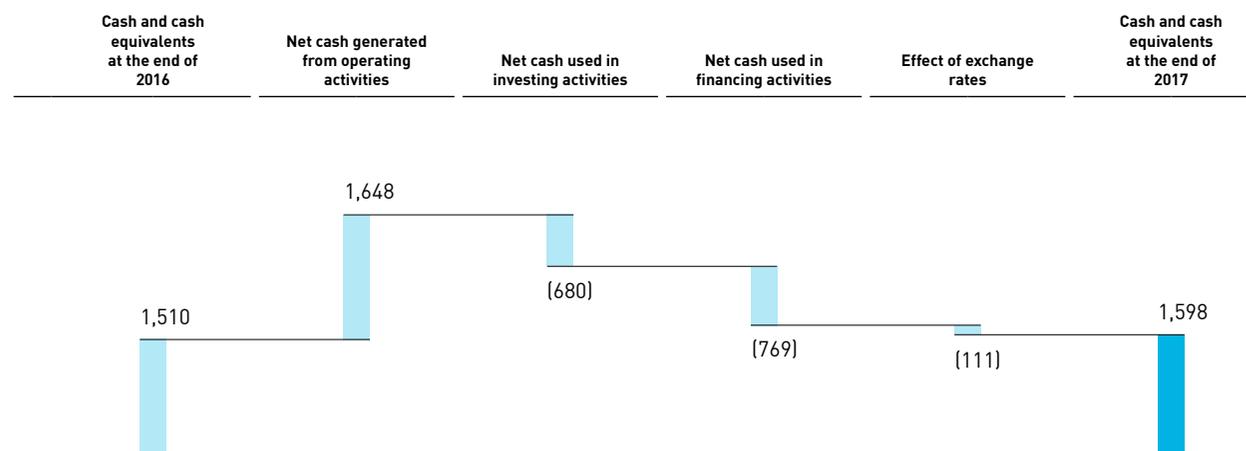
OFF-BALANCE SHEET ITEMS

The company's most significant off-balance sheet items are commitments for promotion and advertising as well as operating leases, which are related to own-retail stores, offices, warehouses and equipment. The company has entered into various operating leases as opposed to property acquisitions in order to reduce exposure to property value fluctuations. Minimum future lease payments for operating leases were € 2.649 billion at December 31, 2017, compared to € 2.501 billion at the end of December 2016, representing an increase of 6%. [SEE NOTE 29, P. 189](#) At the end of December 2017, financial commitments for promotion and advertising decreased 7% to € 5.255 billion in 2017 (2016: € 5.643 billion).

[SEE NOTE 39, P. 210](#)

Change in cash and cash equivalents € in millions

74



TREASURY

CORPORATE FINANCING POLICY

In order to be able to meet the company's payment commitments at all times, the major goal of our financing policy is to ensure sufficient liquidity reserves, while at the same time minimizing our financial expenses. The operating activities of our segments and the resulting cash inflows represent the company's main source of liquidity. Liquidity is planned on a rolling monthly basis under a multi-year financial and liquidity plan. This comprises all consolidated companies. Our in-house bank concept takes advantage of any surplus funds of individual companies to cover the financial requirements of others, thus reducing external financing needs and optimizing our net interest expenses. Furthermore, by settling intercompany transactions via intercompany financial accounts, we are able to reduce external bank account transactions and thus bank charges. Effective management of our currency exposure and interest rate risks are additional goals and responsibilities of our centrally managed Treasury department.

TREASURY POLICY AND RESPONSIBILITIES

Our Treasury Policy governs all treasury-related issues, including banking policy and approval of bank relationships, financing arrangements and liquidity/asset management, currency and interest risk management as well as the management of intercompany cash flows. Responsibilities are arranged in a three-tiered approach:

- The Treasury Committee consists of members of the Executive Board and other senior executives who decide on the Treasury Policy and provide strategic guidance for managing treasury-related topics. Major changes to our Treasury Policy are subject to the prior approval of the Treasury Committee.

- The Treasury department is responsible for specific centralized treasury transactions and for the global implementation of our Treasury Policy.
- On a subsidiary level, where applicable and economically reasonable, local managing directors and finance directors are responsible for managing treasury matters in their respective subsidiaries. Controlling functions on a corporate level ensure that the transactions of the individual business units are in compliance with our Treasury Policy.

CENTRALIZED TREASURY FUNCTION

In accordance with our Treasury Policy, all worldwide credit lines are directly or indirectly managed by the Treasury department. Portions of those lines are allocated to our subsidiaries and backed by adidas AG guarantees. As a result of this centralized liquidity management, the company is well positioned to allocate resources efficiently throughout the organization. The company's debt is generally unsecured and may include standard covenants, which are reviewed on a quarterly basis. We maintain good relations with numerous partner banks, thereby avoiding a high dependency on any single financial institution. Banking partners of the company and our subsidiaries are required to have at least a BBB+ long-term investment grade rating by Standard & Poor's or an equivalent rating by another leading rating agency. [SEE RISK AND OPPORTUNITY REPORT, P. 131](#) Only in exceptional cases are our companies authorized to work with banks with a lower rating. To ensure optimal allocation of the company's liquid financial resources, subsidiaries transfer excess cash to our headquarters in all instances where it is legally and economically feasible. In this regard, the standardization and consolidation of our global cash management and payment processes, including automated domestic and cross-border *cash pools* [SEE GLOSSARY](#), is a key priority for our Treasury department.

STANDARD COVENANTS

In the case of our committed credit facilities, we have entered into various legal covenants. These legal covenants may include limits on the disposal of fixed assets, the amount of debt secured by liens, cross default provisions and change of control. However, our financial arrangements do not contain any financial covenants. If we failed to meet any covenant and were unable to obtain a waiver from a majority of partner banks, borrowings would become due and payable immediately. As at December 31, 2017, we were in full compliance with all of our covenants. We are fully confident we will continue to be compliant with these covenants going forward. We believe that cash generated from operating activities, together with access to internal and external sources of funds, will be sufficient to meet our future operating and capital needs.

FINANCIAL FLEXIBILITY

The company's financial flexibility is ensured by the availability of credit facilities, consisting of committed and uncommitted bilateral credit lines at different banks with a remaining time to maturity of up to five years. In addition, we have an unused multi-currency commercial paper program in the amount of € 2.0 billion available (2016: € 2.0 billion). At the end of 2017, committed and uncommitted bilateral credit lines amounted to € 2.251 billion (2016: € 2.403 billion), of which € 2.145 billion was unutilized (2016: € 2.024 billion). Committed and uncommitted credit lines represent approximately 47% and 53% of total short-term bilateral credit lines, respectively (2016: 43% and 57%, respectively). [SEE DIAGRAM 77](#) We monitor the ongoing need for available credit lines based on the current level of debt as well as future financing requirements.

Total credit facilities € in millions 75

	2017	2016
Bilateral credit lines	2,251	2,403
Eurobonds	983	982
Convertible bond	31	257
Total	3,265	3,642

Remaining time to maturity of available facilities € in millions 76

	2017	2016
< 1 year	1,601	2,160
1 to 3 years	381	150
3 to 5 years	746	945
> 5 years	537	387
Total	3,265	3,642

Bilateral credit lines € in millions 77

	2017	2016
Committed	1,055	1,041
Uncommitted	1,196	1,362
Total	2,251	2,403

OUTSTANDING BONDS

In 2014, we issued two eurobonds with an overall volume of € 1.0 billion, thereby taking the opportunity of a low interest rate environment in the eurobond market to further strengthen the company's financing mix while increasing the overall duration. The seven-year eurobond of € 600 million matures on October 8, 2021 and has a coupon of 1.25%. The twelve-year eurobond of € 400 million matures on October 8, 2026 and has a coupon of 2.25%. [SEE NOTE 18, P. 175](#) In addition, adidas AG successfully issued a convertible bond in March 2012, for an aggregate nominal amount of € 500 million, due on June 14, 2019. The bonds were priced with a 0.25% annual coupon and a conversion premium of 40% above the reference price of € 59.61. As at December 31, 2017, 94% of the convertible bond was converted (2016: 48%). [SEE OUR SHARE, P. 57](#)

[SEE TABLE 78](#)**Issued bonds at a glance € in millions** 78

	Volume	Coupon	Maturity
Convertible bond	€ 500	fixed	2019
Eurobond	€ 600	fixed	2021
Eurobond	€ 400	fixed	2026

GROSS BORROWINGS DECREASE

The company's gross borrowings are composed of bank borrowings as well as the outstanding eurobonds and the convertible bond. Gross borrowings decreased 31% to € 1.120 billion at the end of 2017 from € 1.618 billion in the prior year. This development was mainly due to the conversion of convertible bonds and a decrease in short-term bank borrowings. Bank borrowings amounted to € 106 million compared to € 379 million in the prior year. Convertible bonds outstanding decreased 88% to € 31 million from € 257 million in the prior year. This was a result of further conversions into adidas AG shares that occurred in the course of 2017, partly offset by an increase in the convertible bond's debt component.

[SEE OUR SHARE, P. 57](#) The conversions were done on a non-cash basis using treasury shares. The debt component was fully accrued to its nominal value by the end of 2017. Including the company's eurobonds, the total amount of bonds outstanding at the end of 2017 was € 1.014 billion (2016: € 1.239 billion).

[SEE TABLE 79](#)**Financing structure € in millions** 79

	2017	2016
Cash and short-term financial assets	1,604	1,515
Bank borrowings	106	379
Eurobonds	983	982
Convertible bond	31	257
Gross total borrowings	1,120	1,618
Net cash/(net borrowings)	484	(103)

EURO DOMINATES CURRENCY MIX

The vast majority of our gross borrowings are denominated in euros. At the end of 2017, gross borrowings denominated in euros accounted for 91% of total gross borrowings (2016: 77%). [SEE DIAGRAM 80](#)

Currency split of gross borrowings € in millions 80

	2017	2016
EUR	1,016	1,242
USD	2	157
All others	102	219
Total	1,120	1,618

■ 2017 ■ 2016

STABLE DEBT MATURITY PROFILE

Over the course of 2017, the company's financing maturity profile remained stable. In 2018, assuming unchanged maturities, debt instruments of € 137 million will mature, of which € 31 million consists of the anticipated conversions. This compares to € 606 million which matured during the course of 2017. [SEE DIAGRAM 81](#)

Remaining time to maturity of gross borrowings € in millions 81

	2017	2016
< 1 year	137	636
1 to 3 years	-	-
3 to 5 years	596	595
> 5 years	387	387
Total	1,120	1,618

■ 2017 ■ 2016

NET CASH POSITION OF € 484 MILLION

Net cash at December 31, 2017 amounted to € 484 million, compared to net borrowings of € 103 million in 2016, representing an improvement of € 587 million versus the prior year. [SEE DIAGRAM 82](#) This development was driven by the increase in cash generated from operating activities as well as proceeds arising from the disposal of the TaylorMade and CCM Hockey businesses, partly offset by the utilization of cash for the purchase of fixed assets as well as the dividend paid to shareholders and the repurchase of adidas AG shares. In addition, the conversion of convertible bonds into adidas AG shares also contributed to this improvement.

Net cash/(net borrowings)¹ € in millions 82

2017	484
2016	(103)
2015	(460)
2014	(185)
2013	295

¹ Net cash/Net borrowings = cash and cash equivalents + short-term financial assets – short-term borrowings – long-term borrowings.

INTEREST RATE INCREASES

The weighted average interest rate on the company's gross borrowings increased to 2.7% in 2017 (2016: 2.3%). [SEE DIAGRAM 83](#) This development was mainly due to conversions of the convertible bond into adidas AG shares and a reduction in short-term borrowings. Fixed-rate financing represented 91% of total gross borrowings at the end of 2017 (2016: 77%). Variable-rate financing accounted for 9% of total gross borrowings at the end of the year (2016: 23%).

Interest rate development¹ in % 83

2017	2.7
2016	2.3
2015	2.4
2014	3.1
2013	3.8

¹ Weighted average interest rate of gross borrowings.

**EFFECTIVE FOREIGN EXCHANGE MANAGEMENT
A KEY PRIORITY**

As a globally operating company, adidas is exposed to currency risks. Therefore, effective currency management is a key focus of our Treasury department, with the aim of reducing the impact of currency fluctuations on non-euro-denominated net future cash flows. In this regard, hedging US dollars is a central part of our program. This is a direct result of our Asian-dominated sourcing, which is largely denominated in US dollars. [SEE GLOBAL OPERATIONS, P. 74](#) In 2017, our Treasury department managed a net deficit of around US \$ 6.6 billion related to operational activities (2016: US \$ 6.5 billion). Thereof, around US \$ 3.8 billion was against the euro (2016: US \$ 3.5 billion). As governed by our Treasury Policy, we have established a hedging system on a rolling basis up to 24 months in advance, under which the vast majority of the anticipated seasonal hedging volume is secured approximately six months prior to the start of a season. In rare instances, hedges are contracted beyond the 24-month horizon. We had largely covered our anticipated hedging needs for 2018 as of year-end 2017. At the same time, we have already started hedging our exposure for 2019. The use or combination of different hedging instruments, such as forward exchange contracts, currency options and swaps, protects us against unfavorable currency movements.

[SEE RISK AND OPPORTUNITY REPORT, P. 131](#)

FINANCIAL STATEMENTS AND MANAGEMENT REPORT OF ADIDAS AG

adidas AG is the parent company of the adidas Group. It includes operating business functions, primarily for the German market, as well as corporate headquarter functions such as Marketing, Treasury, Taxes, Legal and Finance. adidas AG also administers the company's shareholdings.

OPERATING ACTIVITIES AND CAPITAL STRUCTURE OF ADIDAS AG

The majority of the operating business of adidas AG consists of the sale of merchandise to wholesale partners and own-retail activities.

In addition to its own trading activities, the results of adidas AG are significantly influenced by its holding function for the company as a whole. This is reflected primarily in currency effects, transfer of costs for services provided, interest result and income from investments in related companies.

The opportunities and risks as well as the future development of adidas AG largely reflect those of the company as a whole.

■ [SEE SUBSEQUENT EVENTS AND OUTLOOK, P. 128](#)

■ [SEE RISK AND OPPORTUNITY REPORT, P. 131](#)

The asset and capital structure of adidas AG is significantly impacted by its holding and financing function for the company. For example, 49% of total assets as at December 31, 2017 related to financial assets (2016: 53%), which primarily consist of shares in affiliated companies. Intercompany accounts, through which transactions between affiliated companies are settled, represent another 35% of total assets (2016: 35%) and 48% of total equity and liabilities as at December 31, 2017 (2016: 45%).

PREPARATION OF ACCOUNTS

Unlike the consolidated financial statements, which are in conformity with the International Financial Reporting Standards (IFRS), as adopted by the European Union as at December 31, 2017, the following financial statements of adidas AG have been prepared in accordance with the rules set out in the German Commercial Code (Handelsgesetzbuch – HGB).

INCOME STATEMENT

Statement of income in accordance with
HGB (Condensed) € in millions 84

	2017	2016
Net sales	3,732	3,289
Total output	3,732	3,289
Other operating income	503	439
Cost of materials	(1,292)	(1,127)
Personnel expenses	(692)	(588)
Depreciation and amortization	(91)	(100)
Other operating expenses	(2,170)	(1,803)
Operating profit	(10)	110
Financial result	655	600
Taxes	(96)	(93)
Net income	549	617
Retained earnings brought forward	24	322
Allocation to other revenue reserves	0	(300)
Utilization for the repurchase of treasury shares	0	(11)
Retained earnings	573	629

adidas AG net sales € in millions 85

	2017	2016
Royalty and commission income	1,809	1,580
adidas Germany	1,027	939
Foreign subsidiaries	175	137
Y-3	98	89
Other revenues	623	544
Total	3,732	3,289

NET SALES INCREASE 13%

Sales of adidas AG comprise external revenues generated by adidas Germany with products of the adidas and Reebok brands, external revenues from Y-3 products as well as revenues from foreign subsidiaries. Revenues of adidas AG also include royalty and commission income, mainly from affiliated companies, and other revenues. In 2017, adidas AG net sales grew 13% to € 3.732 billion (2016: € 3.289 billion). This growth was mainly due to an increase in royalty income from affiliated companies as well as higher sales at adidas Germany. ■ [SEE TABLE 85](#)

OTHER OPERATING INCOME UP 15%

In 2017, other operating income of adidas AG increased 15% to € 503 million (2016: € 439 million). This development was primarily due to positive currency effects.

OTHER OPERATING EXPENSES INCREASE 20%

In 2017, other operating expenses for adidas AG rose 20% to € 2.170 billion (2016: € 1.803 billion). ■ [SEE TABLE 84](#) This was largely attributable to an increase in expenses for advertising and promotion, allowances for doubtful accounts, negative currency effects and higher legal and consultancy expenses.

DEPRECIATION AND AMORTIZATION DECLINES 9%

Depreciation and amortization for adidas AG decreased 9% to € 91 million in 2017 (2016: € 100 million), mainly as a result of a decline in depreciation and amortization of software.

**OPERATING RESULT DECREASES
SIGNIFICANTLY**

In 2017, adidas AG generated an operating loss of € 10 million, (2016: operating profit of € 110 million). [SEE TABLE 84](#) This development was primarily due to an increase in other operating expenses as well as increases in cost of materials and personnel expenses, which more than offset higher sales.

FINANCIAL RESULT IMPROVES

The financial result of adidas AG improved 9% to € 655 million in 2017 (2016: € 600 million). The increase was attributable to higher profit transfers from affiliated companies under profit and loss transfer agreements.

NET INCOME DECLINES

Net income, after taxes of € 96 million (2016: € 93 million), amounted to € 549 million in 2017 and was thus 11% below the prior year level (2016: € 617 million). [SEE TABLE 84](#)

BALANCE SHEET

Balance sheet in accordance with HGB
(Condensed) € in millions **86**

	Dec. 31, 2017	Dec. 31, 2016
Assets		
Intangible assets	124	112
Property, plant and equipment	610	493
Financial assets	4,308	4,205
Fixed assets	5,042	4,810
Inventories	49	50
Receivables and other assets	3,262	2,968
Cash and cash equivalents, securities	337	28
Current assets	3,648	3,046
Prepaid expenses	168	143
Active difference from asset allocation	5	4
Total assets	8,863	8,003
Equity and liabilities		
Shareholders' equity	2,704	2,395
Provisions	624	525
Liabilities and other items	5,535	5,083
Total equity and liabilities	8,863	8,003

TOTAL ASSETS ABOVE PRIOR YEAR

At the end of December 2017, total assets grew 11% to € 8.863 billion compared to € 8.003 billion in the prior year. This development was mainly a result of increases in cash and cash equivalents, receivables and other assets as well as fixed assets.

[SEE TABLE 86](#)

SHAREHOLDERS' EQUITY UP 13%

Shareholders' equity increased 13% to € 2.704 billion at the end of December 2017 (2016: € 2.395 billion). [SEE TABLE 86](#) The equity ratio rose slightly to 30.5% (2016: 29.9%).

PROVISIONS INCREASE 19%

Provisions were up 19% to € 624 million at the end of 2017 (2016: € 525 million). [SEE TABLE 86](#) The increase primarily resulted from higher provisions for personnel as well as higher marketing provisions.

LIABILITIES AND OTHER ITEMS UP 9%

At the end of December 2017, liabilities and other items increased 9% to € 5.535 billion (2016: € 5.083 billion). [SEE TABLE 86](#) The increase was mainly a result of higher payables to affiliated companies, partly offset by the decline in liabilities related to the convertible bond.

BUSINESS PERFORMANCE
Disclosures pursuant to § 315a Section 1
and § 289a Section 1 of the German
Commercial Code

CASH INFLOW FROM OPERATING ACTIVITIES REFLECTS CHANGE IN CASH AND CASH EQUIVALENTS

adidas AG generated a positive cash flow from operating activities of € 1.109 billion (2016: € 263 million). The change versus the prior year was mainly a result of higher payables to affiliated companies, partly offset by an increase in receivables from affiliated companies. Net cash outflow from investment activities was € 330 million (2016: € 133 million). This was primarily attributable to capital expenditure for tangible fixed assets of € 227 million and capital expenditure for financial assets in an amount of € 115 million, partly offset by disposals from financial assets of € 12 million. Financing activities resulted in a net cash outflow of € 469 million (2016: € 549 million). The net cash outflow from financing activities mainly relates to the dividend payment in an amount of € 405 million. As a result of all these developments, cash and cash equivalents of adidas AG increased to € 337 million at the end of December 2017 compared to € 28 million at the end of the prior year.

adidas AG has bilateral credit lines of € 1.7 billion. In addition, the company has a multi-currency commercial paper program in an amount of € 2.0 billion. [SEE TREASURY, P. 115](#)

adidas AG is able to meet its financial commitments at all times.

DISCLOSURES PURSUANT TO § 315A SECTION 1 AND § 289A SECTION 1 OF THE GERMAN COMMERCIAL CODE

COMPOSITION OF SUBSCRIBED CAPITAL

The nominal capital of adidas AG amounts to € 209,216,186 (as at December 31, 2017) and is divided into the same number of registered no-par-value shares with a pro rata amount in the nominal capital of € 1 each ('shares'). Pursuant to § 4 section 10 of the Articles of Association, shareholders' claims to the issuance of individual share certificates are, in principle, excluded. Each share grants one vote at the Annual General Meeting. All shares carry the same rights and obligations. As at December 31, 2017, adidas AG held 5,354,952 treasury shares, which however do not confer any rights to the company in accordance with § 71b German Stock Corporation Act (Aktiengesetz – AktG). [SEE NOTE 26, P. 182](#)

In the USA, we have issued American Depositary Receipts (ADRs). ADRs are deposit certificates of non-US shares that are traded instead of the original shares on US stock exchanges. Two ADRs equal one share. [SEE OUR SHARE, P. 57](#)

RESTRICTIONS ON VOTING RIGHTS OR TRANSFER OF SHARES

We are not aware of any contractual agreements with adidas AG or other agreements restricting voting rights or the transfer of shares. Based on the Code of Conduct in conjunction with an internal guideline of adidas AG and based on Article 19 section 11 of the Market Abuse Regulation, however, particular lock-up periods do exist for members of the Executive Board with regard to the purchase and sale of adidas AG shares. These lock-up periods are connected, in particular, with the (time of) publication of quarterly and full year results. Lock-up periods stipulated in the Code of Conduct and the internal guideline also exist for employees who have access to yet unpublished financial results.

In addition, restrictions of voting rights may exist pursuant, inter alia, to § 136 AktG or for treasury shares pursuant to § 71b AktG as well as due to capital market regulations, in particular pursuant to §§ 21 et seq. German Securities Trading Act (Wertpapierhandelsgesetz – WpHG).

The shares that were issued in the context of the Stock Purchase Plan to employees of adidas AG and employees of subsidiaries participating in the Stock Purchase Plan are not subject to any lock-up periods, unless such a waiting period is stipulated in locally applicable regulations. Employees who hold the shares which they purchased themselves (investment shares) for at least one year will subsequently receive one share for every six investment shares without having to pay for such share (so-called matching share) if they are still adidas employees at that point in time. If employees transfer, pledge or hypothecate investment shares in any way during the one-year vesting period, the right to receive matching shares shall cease.

SHAREHOLDINGS IN SHARE CAPITAL EXCEEDING 10% OF VOTING RIGHTS

We have not been notified of, and are not aware of, any direct or indirect shareholdings in the share capital of adidas AG exceeding 10% of the voting rights.

SHARES WITH SPECIAL RIGHTS

There are no shares bearing special rights. In particular, there are no shares with rights conferring powers of control.

VOTING RIGHT CONTROL IF EMPLOYEES HAVE A SHARE IN THE CAPITAL

Like all other shareholders, employees who hold adidas AG shares exercise their control rights directly in accordance with statutory provisions and the Articles of Association. The shares which employees acquire in the context of the Stock Purchase Plan are held in trust centrally by a service provider

on behalf of the participating employees. As long as the shares are held in trust, the trustee shall take reasonable measures to allow participating employees to directly or indirectly exercise their voting rights in respect of the shares held in trust.

EXECUTIVE BOARD APPOINTMENT AND DISMISSAL

Pursuant to § 6 of the Articles of Association and § 84 AktG, the Supervisory Board is responsible for determining the exact number of members of the Executive Board, for their appointment and dismissal as well as for the appointment of the Chief Executive Officer (CEO). The adidas AG Executive Board, which, as a basic principle, comprises at least two members, currently consists of the CEO as well as five further members. Executive Board members may be appointed for a maximum period of five years. Such appointments may be renewed and the terms of office may be extended, provided that no term exceeds five years. [SEE EXECUTIVE BOARD, P. 20](#)

The Supervisory Board may revoke the appointment of an individual as member of the Executive Board or CEO for good cause, such as gross negligence of duties or a vote of no confidence by the Annual General Meeting.

As adidas AG is subject to the regulations of the German Co-Determination Act (Mitbestimmungsgesetz – MitbestG), the appointment of Executive Board members and also their dismissal requires a majority of at least two thirds of the Supervisory Board members (§ 31 MitbestG). If such a majority is not established in the first vote by the Supervisory Board, the Mediation Committee has to present a proposal which, however, does not exclude other proposals. The appointment or dismissal is then made in a second vote with a simple majority of the votes cast by the Supervisory Board members. Should the required majority not be established in this case either, a third vote, again requiring a simple majority, must be

held in which, however, the Chairman of the Supervisory Board has two votes.

If the Executive Board does not have the required number of members, the competent court shall, in urgent cases, make the necessary appointment upon application by any party involved (§ 85 section 1 AktG).

AMENDMENTS TO THE ARTICLES OF ASSOCIATION

Pursuant to § 179 section 1 sentence 1 AktG, the Articles of Association of adidas AG can, in principle, only be amended by a resolution passed by the Annual General Meeting. Pursuant to § 21 section 3 of the Articles of Association in conjunction with § 179 section 2 sentence 2 AktG, the Annual General Meeting of adidas AG principally resolves upon amendments to the Articles of Association with a simple majority of the votes cast and with a simple majority of the nominal capital represented when passing the resolution. However, if mandatory legal provisions stipulate a larger majority of voting rights or capital, this is applicable. When it comes to amendments solely relating to the wording, the Supervisory Board is authorized to make these modifications in accordance with § 179 section 1 sentence 2 AktG in conjunction with § 10 section 1 sentence 2 of the Articles of Association.

AUTHORIZATIONS OF THE EXECUTIVE BOARD

The authorizations of the Executive Board are regulated by §§ 76 et seq. AktG in conjunction with §§ 7 and 8 of the Articles of Association. The Executive Board is responsible, in particular, for managing the company and represents the company judicially and extra-judicially.

AUTHORIZATION OF THE EXECUTIVE BOARD TO ISSUE SHARES

The authorization of the Executive Board to issue shares is regulated by § 4 of the Articles of Association and by statutory provisions:

Authorized Capital

- Until June 7, 2020, the Executive Board is authorized to increase the nominal capital, subject to Supervisory Board approval, by issuing new shares against contributions in kind once or several times by no more than € 16,000,000 altogether (Authorized Capital 2017/II).
- Until June 14, 2021, the Executive Board is authorized to increase the nominal capital, subject to Supervisory Board approval, by issuing new shares against contributions in cash once or several times by no more than € 4,000,000 altogether (Authorized Capital 2016).
- Until June 7, 2022, the Executive Board is authorized to increase the nominal capital, subject to Supervisory Board approval, by issuing new shares against contributions in cash once or several times by no more than € 50,000,000 altogether (Authorized Capital 2017/I).
- Until June 7, 2022, the Executive Board is authorized to increase the nominal capital, subject to Supervisory Board approval, by issuing new shares against contributions in cash once or several times by no more than € 20,000,000 altogether (Authorized Capital 2017/III).

Subject to Supervisory Board approval, shareholders' subscription rights are partially excluded or may be excluded in certain cases for the above-mentioned, in principle cumulative authorizations. [SEE NOTE 26, P. 182](#)

Contingent Capital

- The nominal capital of the company is conditionally increased by up to € 36,000,000 (Contingent Capital 2010). The Contingent Capital serves the purpose of granting

holders or creditors of bonds that were issued up to May 5, 2015 based on the resolution of the Annual General Meeting on May 6, 2010 subscription or conversion rights relating to no more than a total of 36,000,000 shares in compliance with the corresponding conditions of the bonds.

On March 14, 2012, following the approval of the Supervisory Board, the Executive Board resolved to make partial use of the authorization granted by the Annual General Meeting on May 6, 2010 and issued a convertible bond, excluding shareholders' subscription rights, on March 21, 2012. However, the shares will only be issued insofar as bondholders make use of their conversion rights. The total number of shares to be issued to bondholders in case of full conversion amounted to up to 3,182,525 shares as at December 31, 2016. Due to the fact that conversion rights were exercised, which were all serviced with treasury shares of the company, the remaining number of shares to be issued to bondholders in case of full conversion amounted to up to 377,190 shares as at December 31, 2017.

Moreover, the authorization to issue bonds with warrants and/or convertible bonds granted on May 6, 2010 was canceled by resolution of the Annual General Meeting on May 8, 2014.

- Furthermore, the nominal capital of the company is conditionally increased by up to € 12,500,000 (Contingent Capital 2014). The Contingent Capital serves the purpose of granting holders or creditors of bonds that were issued based on the resolution of the Annual General Meeting on May 8, 2014 subscription or conversion rights relating to no more than a total of 12,500,000 shares in compliance with the corresponding conditions of the bonds. Based on the authorization granted by the Annual General Meeting on May 8, 2014, the Executive Board is authorized, subject to Supervisory Board approval, to issue bonds with warrants and/or convertible bonds in an aggregate

nominal value of up to € 1,000,000,000 with or without a limited term, against contributions in cash once or several times until May 7, 2019, and to guarantee bonds issued by subordinated Group companies. The Executive Board is also authorized, subject to Supervisory Board approval, to exclude shareholders' subscription rights for fractional amounts and to exclude shareholders' subscription rights insofar as this is necessary for granting subscription rights to which holders or creditors of previously issued bonds are entitled. Furthermore, the Executive Board is authorized, subject to Supervisory Board approval, to also exclude shareholders' subscription rights if the issue price of the bonds is not significantly below the hypothetical market value of these bonds and the number of shares to be issued does not exceed 10% of the nominal capital. The issuance of new shares or the use of treasury shares must be taken into account when calculating the limit of 10% in certain specific cases.

The Executive Board has so far not utilized the authorization to issue bonds with warrants and/or convertible bonds granted by the Annual General Meeting on May 8, 2014.

AUTHORIZATION OF THE EXECUTIVE BOARD TO REPURCHASE SHARES

The authorizations of the Executive Board to repurchase adidas AG shares arise from §§ 71 et seq. AktG and, as at the balance sheet date, from the authorization granted by the Annual General Meeting on May 12, 2016.

- Until May 11, 2021, the Executive Board is authorized to repurchase adidas AG shares in an amount totaling up to 10% of the nominal capital at the date of the resolution (or, as the case may be, a lower amount of nominal capital at the date of utilization of the authorization) for any lawful purpose and within the legal framework. The authorization may be used by the company but also by its subordinated

Group companies or by third parties on account of the company or its subordinated Group companies or third parties assigned by the company or one of its subordinated Group companies.

The repurchase can be carried out via the stock exchange, through a public invitation to submit sale offers, through a public repurchase offer, or through granting tender rights to shareholders. Furthermore, the authorization sets out the lowest and highest nominal value that may be granted in each case.

The purposes for which adidas AG shares repurchased based on this authorization may be used are set out in the resolution on Item 9 of the Agenda for the Annual General Meeting held on May 12, 2016. The shares may in particular be used as follows:

- They may be sold via the stock exchange, through a public share purchase offer made to all shareholders or sold otherwise against cash (limited to 10% of the nominal capital taking into account certain offsets) at a price not significantly below the stock market price of shares with the same features.
- They may be offered and assigned as consideration for the direct or indirect acquisition of companies, parts of companies, participations in companies or other economic assets or within the scope of company mergers.
- They may be offered and sold as consideration for the acquisition of industrial property rights or intangible property rights or for the acquisition of licenses relating to such rights, also through subordinated Group companies.
- They may be used for purposes of meeting the subscription or conversion rights or obligations or the company's right to delivery of shares arising from

BUSINESS PERFORMANCE
Disclosures pursuant to § 315a Section 1
and § 289a Section 1 of the German
Commercial Code

bonds with warrants and/or convertible bonds issued by the company or its subordinated Group companies.

- In connection with employee stock purchase plans, up to 4,000,000 shares may be issued in favor of (current or former) employees of the company and its affiliated companies as well as in favor of (current and former) management bodies of the company's affiliated companies.
- They may be canceled without requiring an additional resolution of the Annual General Meeting.

Furthermore, the shares may be assigned to members of the Executive Board as compensation by way of a stock bonus subject to the provision that resale by the Executive Board members shall only be permitted following a retention period of at least three years from the date of assignment. Responsibility in this case lies with the Supervisory Board.

In case of utilization of shares for the above-mentioned purposes, except for the cancelation of shares, shareholders' subscription rights are excluded.

The Supervisory Board may provide that transactions based on this authorization may only be carried out subject to the approval of the Supervisory Board or one of its committees.

In the year under review, the Executive Board partly utilized the authorization to repurchase treasury shares. In a third tranche (total period from November 8, 2016 up to and including January 31, 2017) of the share buyback program, adidas AG bought back 472,966 treasury shares via the stock exchange in the period from January 1, 2017 up to and including January 31, 2017. [SEE NOTE 26, P. 182](#)

- In the scope of the authorization resolved by the Annual General Meeting on May 12, 2016, the Executive Board is furthermore authorized to conduct the share buyback

also by using equity derivatives which are arranged with a credit institution or financial services institution in close conformity with market conditions. adidas AG may acquire call options issued for physical delivery and/or sell put options or use a combination of call and put options or other equity derivatives if the option conditions ensure that these shares are only delivered if they were purchased in compliance with the equality principle. All share purchases using the aforementioned equity derivatives are limited to a maximum value of 5% of the nominal capital existing at the date on which the resolution was adopted by the Annual General Meeting (or, as the case may be, a lower amount of nominal capital at the date of utilization of the authorization). The term of the options may not exceed 18 months and must furthermore be chosen in such a way that the shares are acquired upon the exercise of the options no later than May 11, 2021. The authorization furthermore sets out the lowest and highest nominal value that may be granted in each case.

For excluding subscription rights, the use and cancelation of shares purchased using equity derivatives, the general provisions adopted by the Annual General Meeting (set out above) are applicable accordingly.

CHANGE OF CONTROL/COMPENSATION AGREEMENTS

Material agreements entered into by adidas AG containing a change-of-control clause relate to financing agreements. In the case of a change of control, these agreements, in accordance with common practice, entitle the creditor to termination and early calling-in of any outstanding amounts.

No compensation agreements exist between adidas AG and members of the Executive Board or employees relating to the event of a takeover bid.

BUSINESS PERFORMANCE BY SEGMENT

adidas has divided its operating activities into the following operating segments: Western Europe, North America (excluding USA Reebok), USA Reebok, Greater China, Russia/CIS, Latin America, Japan, Middle East, South Korea and Southeast Asia/Pacific. While the business segments Western Europe, Greater China, Russia/CIS, Latin America and Japan are reported separately, North America (excluding USA Reebok) and USA Reebok are combined to the reportable segment North America. Similarly, the markets Middle East, South Korea and Southeast Asia/Pacific are aggregated to the reportable segment MEAA ('Middle East, Africa and other Asian markets'). Each market comprises all business activities in the wholesale and retail distribution channels of the adidas and Reebok brands. Segmental operating expenses primarily relate to marketing expenditure as well as operating overhead costs.

WESTERN EUROPE

In 2017, sales in Western Europe increased 13% on a currency-neutral basis. In euro terms, sales in Western Europe grew 11% to € 5.883 billion from € 5.291 billion in 2016. Despite difficult prior year comparisons mainly resulting from revenues generated with UEFA EURO 2016 related products as well as the termination of the Chelsea F.C. sponsorship as of June 30, 2016, adidas brand revenues grew 12% on a currency-neutral basis. This development was driven by double-digit sales growth in the running and outdoor categories as well as at adidas Originals and adidas neo. In addition, mid-single-digit increases in the training category also supported this development. Reebok brand revenues in Western Europe increased 24% on a currency-neutral basis, as a result of double-digit sales growth in Classics as well as high-single-digit growth in the training and running categories. [SEE TABLE 87](#)

Gross margin in Western Europe increased 1.1 percentage points to 45.5% from 44.4% in 2016 as positive effects from a more favorable pricing and channel mix more than offset the significant negative impact from unfavorable currency developments as well as higher input costs. Operating expenses were up 7% to € 1.501 billion versus € 1.398 billion in 2016. This development reflects an increase in marketing expenditure as well as higher operating overhead costs. Operating expenses as a percentage of sales were down 0.9 percentage points to 25.5% (2016: 26.4%). The operating margin increased 2.1 percentage points to 20.0% (2016: 18.0%), as a result of the gross margin improvement as well as the positive effect of lower operating expenses as a percentage of sales. Operating profit in Western Europe increased 24% to € 1.178 billion versus € 951 million in the prior year. [SEE TABLE 87](#)

Western Europe at a glance € in millions

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	2017	2016	Change	Change (currency-neutral)
Net sales	5,883	5,291	11%	13%
adidas brand	5,388	4,889	10%	12%
Reebok brand	496	402	23%	24%
Gross profit	2,679	2,350	14%	–
Gross margin	45.5%	44.4%	1.1pp	–
Segmental operating profit	1,178	951	24%	–
Segmental operating margin	20.0%	18.0%	2.1pp	–

NORTH AMERICA

Revenues in North America grew 27% on a currency-neutral basis and 25% in euro terms to € 4.275 billion from € 3.412 billion in 2016. adidas brand sales increased 35% on a currency-neutral basis, driven by double-digit sales growth in the running and training categories as well as at adidas Originals and adidas neo. Revenues of the Reebok brand in North America decreased 15% on a currency-neutral basis, reflecting the closure of own-retail stores in the US. [SEE REEBOK BRAND STRATEGY, P. 70](#) From a category perspective, double-digit growth in Classics was more than offset by sales declines in the training and running categories. [SEE TABLE 88](#)

Gross margin in North America increased 1.8 percentage points to 39.5% (2016: 37.7%) driven by an improved product mix, partly offset by a less favorable channel and pricing mix as well as higher input costs. Operating expenses were up 14% to € 1.280 billion versus € 1.124 billion in 2016, reflecting an increase in marketing expenditure as well as higher operating overhead costs. Operating expenses as a percentage of sales decreased 3.0 percentage points to 29.9% (2016: 32.9%). As a result of the strong top-line development, the

North America at a glance € in millions

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	2017	2016	Change	Change (currency-neutral)
Net sales	4,275	3,412	25%	27%
adidas brand	3,843	2,897	33%	35%
Reebok brand	432	514	(16%)	(15%)
Gross profit	1,689	1,286	31%	–
Gross margin	39.5%	37.7%	1.8pp	–
Segmental operating profit	468	214	119%	–
Segmental operating margin	10.9%	6.3%	4.7pp	–

gross margin increase as well as the positive effect of lower operating expenses as a percentage of sales, the operating margin improved 4.7 percentage points to 10.9% from 6.3% in 2016. Operating profit in North America more than doubled to € 468 million from € 214 million in 2016. [SEE TABLE 88](#)

GREATER CHINA

Sales in Greater China grew 29% on a currency-neutral basis. In euro terms, sales in Greater China were up 26% to € 3.789 billion from € 3.010 billion in 2016. Revenues of brand adidas increased 30% on a currency-neutral basis. This development was due to double-digit sales growth in the running, training and basketball categories as well as at adidas Originals and adidas neo. In addition, the outdoor category, where revenues more than doubled, also contributed to this development. Reebok brand sales in Greater China grew 25% on a currency-neutral basis, driven by double-digit sales increases in the training and running categories as well as in Classics. [SEE TABLE 89](#)

Gross margin in Greater China decreased 0.5 percentage points to 57.1% (2016: 57.5%), as a more favorable product and pricing mix was more than offset by negative currency effects. Operating expenses were up 22% to € 820 million versus € 671 million in 2016. This development reflects an increase in both marketing expenditure as well as operating overhead costs. Operating expenses as a percentage of sales declined 0.6 percentage points to 21.7% (2016: 22.3%). As a result of lower operating expenses as a percentage of sales, which more than offset the decline in gross margin, the operating margin improved 0.2 percentage points to 35.4% versus 35.2% in 2016. Operating profit in Greater China increased 27% to € 1.342 billion from € 1.060 billion in 2016.

[SEE TABLE 89](#)

Greater China at a glance € in millions

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	2017	2016	Change	Change (currency-neutral)
Net sales	3,789	3,010	26%	29%
adidas brand	3,707	2,944	26%	30%
Reebok brand	82	67	23%	25%
Gross profit	2,162	1,731	25%	–
Gross margin	57.1%	57.5%	(0.5pp)	–
Segmental operating profit	1,342	1,060	27%	–
Segmental operating margin	35.4%	35.2%	0.2pp	–

RUSSIA/CIS

Sales in Russia/CIS decreased 13% on a currency-neutral basis, reflecting the significant number of store closures in 2017. In euro terms, sales in Russia/CIS declined 3% to € 660 million from € 679 million in 2016. adidas brand revenues were down 16% on a currency-neutral basis, due to sales declines in most categories. Revenues of the Reebok brand in Russia/CIS decreased 2% on a currency-neutral basis, as increases in the training category were more than offset by declines in the running category as well as in Classics. [SEE TABLE 90](#)

Gross margin in Russia/CIS increased 6.7 percentage points to 64.9% from 58.1% in 2016, driven by an improved pricing mix as well as significant positive currency effects, which more than offset a less favorable channel mix. Operating expenses were up 1% to € 292 million (2016: € 290 million), reflecting negative currency effects. On a currency-neutral basis, operating expenses declined, due to a decrease in

marketing expenditure as well as lower operating overhead costs. Operating expenses as a percentage of sales increased 1.5 percentage points to 44.3% versus 42.7% in the prior year. As a result of the gross margin increase, which more than offset the negative effect of higher operating expenses as a percentage of sales, the operating margin improved 5.2 percentage points to 20.6% from 15.4% in 2016. Operating profit in Russia/CIS increased 30% to € 136 million versus € 105 million in 2016. [SEE TABLE 90](#)

Russia/CIS at a glance € in millions

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	2017	2016	Change	Change (currency-neutral)
Net sales	660	679	(3%)	(13%)
adidas brand	478	514	(7%)	(16%)
Reebok brand	182	166	10%	(2%)
Gross profit	429	395	8%	–
Gross margin	64.9%	58.1%	6.7pp	–
Segmental operating profit	136	105	30%	–
Segmental operating margin	20.6%	15.4%	5.2pp	–

LATIN AMERICA

Revenues in Latin America increased 12% on a currency-neutral basis and 10% in euro terms to € 1.907 billion from € 1.731 billion in 2016. Revenues of brand adidas were up 12% on a currency-neutral basis. This development was driven by double-digit sales growth at adidas Originals and adidas neo. In addition, mid-single-digit increases in the football category also contributed to this development. Reebok brand sales in Latin America grew 12% on a currency-neutral basis, driven by double-digit growth in the training category as well as in Classics. [SEE TABLE 91](#)

Gross margin in Latin America decreased 0.3 percentage points to 42.1% (2016: 42.4%), as the positive effects from a more favorable pricing, channel and product mix were more than offset by significant negative currency effects as well as higher input costs. Operating expenses increased 6% to € 535 million from € 507 million in 2016, reflecting an increase in both marketing expenditure as well as operating overhead costs. Operating expenses as a percentage of sales declined 1.2 percentage points to 28.1% (2016: 29.3%). As a result of lower operating expenses as a percentage of sales, which

more than offset the decline in gross margin, the operating margin increased 0.9 percentage points to 14.0% from 13.1% in 2016. Operating profit in Latin America increased 18% to € 268 million versus € 227 million in 2016. [SEE TABLE 91](#)

JAPAN

Sales in Japan grew 10% on a currency-neutral basis. In euro terms, revenues in Japan increased 5% to € 1.056 billion from € 1.007 billion in 2016. adidas brand revenues grew 10% on a currency-neutral basis, driven by double-digit sales increases in the running and outdoor categories as well as at adidas neo. In addition, high-single-digit increases in the football category and at adidas Originals as well as mid-single-digit growth in the training category also contributed to this development. Sales of the Reebok brand in Japan were up 6% on a currency-neutral basis, supported by double-digit sales increases in the running and training categories, which more than offset declines in Classics. [SEE TABLE 92](#)

Gross margin in Japan increased 3.7 percentage points to 53.0% versus 49.4% in 2016, driven by a significantly more favorable currency development as well as an improved

pricing and channel mix. This was partly offset by higher input costs as well as a less favorable product mix. Operating expenses were up 2% to € 310 million from € 304 million in 2016, reflecting higher marketing expenditure as well as an increase in operating overhead costs. Operating expenses as a percentage of sales decreased 0.8 percentage points to 29.4% (2016: 30.2%). The operating margin grew 4.6 percentage points to 25.2% versus 20.6% in 2016, as a result of the gross margin increase as well as the positive effect of lower operating expenses as a percentage of sales. Operating profit in Japan increased 28% to € 266 million from € 207 million in 2016. [SEE TABLE 92](#)

MEAA

Revenues in MEAA were up 10% on a currency-neutral basis. In euro terms, sales in MEAA grew 8% to € 2.907 billion from € 2.685 billion in 2016. Sales of the adidas brand increased 11% on a currency-neutral basis, due to double-digit sales growth in the running and outdoor categories as well as at adidas Originals and adidas neo. Reebok brand revenues in MEAA were up 2% on a currency-neutral basis, driven by high-single-digit increases in the training category. [SEE TABLE 93](#)

Latin America at a glance € in millions

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	2017	2016	Change	Change (currency-neutral)
Net sales	1,907	1,731	10%	12%
adidas brand	1,673	1,515	10%	12%
Reebok brand	235	216	9%	12%
Gross profit	803	734	9%	-
Gross margin	42.1%	42.4%	[0.3pp]	-
Segmental operating profit	268	227	18%	-
Segmental operating margin	14.0%	13.1%	0.9pp	-

Japan at a glance € in millions

92

	2017	2016	Change	Change (currency-neutral)
Net sales	1,056	1,007	5%	10%
adidas brand	955	907	5%	10%
Reebok brand	101	100	1%	6%
Gross profit	560	497	13%	-
Gross margin	53.0%	49.4%	3.7pp	-
Segmental operating profit	266	207	28%	-
Segmental operating margin	25.2%	20.6%	4.6pp	-

MEAA at a glance € in millions

93

	2017	2016	Change	Change (currency-neutral)
Net sales	2,907	2,685	8%	10%
adidas brand	2,603	2,385	9%	11%
Reebok brand	304	301	1%	2%
Gross profit	1,514	1,344	13%	-
Gross margin	52.1%	50.0%	2.1pp	-
Segmental operating profit	847	722	17%	-
Segmental operating margin	29.1%	26.9%	2.2pp	-

Gross margin in MEAA increased 2.1 percentage points to 52.1% (2016: 50.0%), driven by an improved pricing, product and channel mix, partly offset by negative currency effects and higher input costs. Operating expenses were up 7% to € 669 million versus € 624 million in 2016, mainly as a result of higher operating overhead costs. As a percentage of sales, operating expenses declined 0.2 percentage points to 23.0% from 23.2% in 2016. The operating margin was up 2.2 percentage points to 29.1% (2016: 26.9%), as a result of the higher gross margin as well as the positive effect of lower operating expenses as a percentage of sales. Operating profit in MEAA increased 17% to € 847 million versus € 722 million in 2016. [■ SEE TABLE 93](#)

SUBSEQUENT EVENTS AND OUTLOOK

In 2018, we expect the global economy and consumer spending to grow, providing a positive backdrop for robust growth and expansion of the sporting goods industry. Through our extensive pipeline of innovative products, powerful brand-building activities and tight control of both our inventory levels and our cost base, we project strong top- and bottom-line improvements in 2018. We forecast sales to increase at a rate of around 10% on a currency-neutral basis. Gross margin is projected to grow up to 0.3 percentage points to a level of up to 50.7%. Operating margin is expected to increase between 0.5 and 0.7 percentage points to a level between 10.3% and 10.5%, driven by the increase in gross margin as well as the positive effect of lower other operating expenses as a percentage of sales. Paired with lower financial expenses and a reduced tax rate, we project net income from continuing operations to increase to a level between € 1.615 billion and € 1.675 billion.

SUBSEQUENT EVENTS

NO SUBSEQUENT EVENTS

Since the end of 2017, there have been no significant organizational, management, economic, sociopolitical, legal or financial changes which we expect to influence our business materially going forward.

OUTLOOK

FORWARD-LOOKING STATEMENTS

This Management Report contains forward-looking statements that reflect Management's current view with respect to the future development of our company. The outlook is based on estimates that we have made on the basis of all the information available to us at the time of completion of this Annual Report. In addition, such forward-looking statements are subject to uncertainties which are beyond the control of the company. [SEE RISK AND OPPORTUNITY REPORT, P. 131](#) In case the underlying assumptions turn out to be incorrect or described risks or opportunities materialize, actual results and developments may materially deviate (negatively or positively) from those expressed by such statements. adidas does not assume any obligation to update any forward-looking statements made in this Management Report beyond statutory disclosure obligations.

CHANGES TO SEGMENTAL REPORTING

To win the consumer in the dynamic Asian business environment and to provide consumers with a consistent best-in-class brand experience across all channels and markets, we aim at further driving simplicity and consistency across Asia. In this context, effective January 1, 2018, we have consolidated our former four Asia/Pacific markets Greater China, Japan, South Korea and Southeast Asia/Pacific to one operating segment Asia/Pacific. By doing so, we will create a more sustainable business model across Asia, in which we will be able to share and implement best practices in a more efficient manner.

Therefore, effective January 1, 2018, adidas has divided its operating activities into the following operating segments:

Western Europe, North America (excluding USA Reebok), USA Reebok, Russia/CIS, Latin America, Asia/Pacific and Emerging Markets. While the business segments Western Europe, Russia/CIS, Latin America, Asia/Pacific and Emerging Markets are reported separately, North America (excluding USA Reebok) and USA Reebok are combined to the reportable segment North America. Each market comprises all business activities in the wholesale and retail distribution channels of the adidas and Reebok brands.

GLOBAL ECONOMY TO GROW STEADILY IN 2018¹

Global GDP is projected to remain on a steady growth trajectory, expanding 3.1% in 2018. The ongoing cyclical recovery is expected to continue, driven by a further acceleration in global trade, on the back of benign global financing conditions, accommodative monetary policies, rising consumer confidence and firming commodity prices. However, the headline growth forecast conceals differences between the pace of growth in developed and developing economies. Developing economies are forecast to see an acceleration of growth to 4.5% as commodity-exporting economies benefit from a stabilization of oil and other commodity prices. In contrast, growth in developed economies is projected to slow to 2.2%, as gradual monetary tightening appears likely and aging populations as well as weak productivity trends impose a constraint on growth. With macroeconomic indicators generally at elevated levels already and potential economic growth set to decrease due to a slowdown in productivity growth as well as less favorable demographic trends, risks to the global outlook are tilted to the downside. A rise in borrowing costs or disorderly movements in financial markets might cause turbulence and potentially derail the expansion. In addition, instances of trade protectionism or geopolitical conflicts could dampen consumer confidence, trade and growth.

¹ Source: World Bank Global Economic Prospects.

SPORTING GOODS INDUSTRY EXPANSION TO CONTINUE IN 2018

In the absence of any major macroeconomic shocks, we expect the global sporting goods industry to grow at a mid-single-digit rate in 2018. Sector growth in North America, the biggest market by size globally, is yet to return to the pace seen in the past. At the same time, most markets globally look set to continue expanding at robust rates. The occurrence of major sports events such as the 2018 FIFA World Cup will provide a modest tailwind to the overall sector. Consumer spending on sporting goods in the developing economies is expected to grow faster than in the more developed markets. Progressing urbanization and a growing middle-class in many developing economies are predicted to further propel industry growth throughout the year. In developed economies, the sporting goods industry is forecast to expand, as wage increases on the back of generally strong labor market conditions will

support consumer spending on sporting goods. Around the world, rising sports participation and health awareness is projected to continue to boost demand for athletic performance products. In addition, sportswear penetration rates are forecast to edge up further as sports-inspired apparel and footwear ('athleisure') has become a structural component of the broader fashion landscape, fueling the demand for athletic casual and activewear products. Within the supply chain, innovation such as the application of new manufacturing techniques is projected to enhance speed-to-market capabilities of sports brands, which will favorably impact sales growth as consumers' demands can be met faster and more precisely. On the distribution side, the e-commerce channel, which is already a significant growth driver for the industry, is anticipated to broaden out further as investments into the digital transformation continue across the sporting goods industry.

CURRENCY-NEUTRAL SALES TO INCREASE AT A RATE OF AROUND 10% IN 2018

We expect sales to increase at a rate of around 10% on a currency-neutral basis in 2018. [SEE TABLE 94](#) Despite continued uncertainties regarding the global economic outlook, the company's sales development will be favorably impacted by rising consumer spending, increasing penetration of sportswear ('athleisure') and growing health awareness in most geographical areas, as well as major events such as the 2018 FIFA World Cup. In addition, the further expansion and improvement of our controlled space initiatives, in particular through our own e-commerce channel, is expected to contribute to sales growth.

NORTH AMERICA AND ASIA/PACIFIC TO GROW AT A DOUBLE-DIGIT CURRENCY-NEUTRAL RATE

In 2018, we expect currency-neutral revenues to increase in most market segments. While currency-neutral sales are projected to grow at double-digit rates in North America and Asia/Pacific, currency-neutral sales in Western Europe and Latin America are forecast to improve at a mid-single-digit rate each. In addition, currency-neutral revenues in Emerging Markets are expected to grow at a low-single-digit rate. Currency-neutral sales in Russia/CIS are expected to be around the prior year level. [SEE TABLE 94](#)

GROSS MARGIN EXPECTED TO INCREASE TO A LEVEL OF UP TO 50.7%

In 2018, the gross margin is forecast to increase up to 0.3 percentage points to a level of up to 50.7% (2017: 50.4%). [SEE TABLE 94](#) Gross margin will benefit from the positive effects of a more favorable pricing, channel and regional mix. These improvements will be partly offset by the negative impact from unfavorable currency movements as well as higher labor expenditures in our sourcing countries and higher commodity prices.

2018 Outlook

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Currency-neutral sales development (in %):	
adidas	to increase at a rate of around 10%
Western Europe ¹	mid-single-digit increase
North America ¹	double-digit increase
Asia/Pacific ¹	double-digit increase
Russia/CIS ¹	around prior year level
Latin America ¹	mid-single-digit increase
Emerging Markets ¹	low-single-digit increase
Gross margin	to increase up to 0.3pp to a level of up to 50.7%
Other operating expenses in % of sales	below prior year level
Operating profit	to increase at a rate between 9% and 13%
Operating margin	to increase between 0.5 and 0.7pp to a level between 10.3% and 10.5%
Net income from continuing operations ²	to increase at a rate between 13% and 17% to a level between € 1.615 billion and € 1.675 billion
Basic earnings per share from continuing operations ²	to increase at a rate between 12% and 16%
Average operating working capital in % of sales	around prior year level
Capital expenditure	to increase to a level of around € 900 million

¹ Combined sales of the adidas and Reebok brands.

² 2017 excluding negative one-time tax impact of € 76 million.

OPERATING MARGIN TO EXPAND TO A LEVEL BETWEEN 10.3% AND 10.5%

In 2018, other operating expenses as a percentage of sales are expected to be below the prior year level of 41.9%. This, together with continued top-line growth and the projected gross margin improvement, is expected to drive an increase in operating profit of between 9% and 13%. Consequently, we expect the operating margin to increase between 0.5 and 0.7 percentage points to a level between 10.3% and 10.5% compared to the prior year level of 9.8%. [SEE TABLE 94](#)

NET INCOME FROM CONTINUING OPERATIONS TO INCREASE BETWEEN 13% AND 17%

Net income from continuing operations is projected to increase to a level between € 1.615 billion and € 1.675 billion. This development reflects an increase of between 13% and 17% compared to the prior year level of € 1.430 billion, excluding the negative one-time tax impact recorded in 2017. Basic earnings per share from continuing operations are expected to increase at a rate between 12% and 16% compared to the prior year level of € 7.05, excluding the negative one-time tax impact in 2017. [SEE TABLE 94](#) Net financial expenses are forecast to decrease in 2018. The tax rate is projected to be below the prior year level of 29.3%, excluding the negative one-time tax impact recorded in 2017.

AVERAGE OPERATING WORKING CAPITAL AS A PERCENTAGE OF SALES TO BE AROUND PRIOR YEAR LEVEL

In 2018, average operating working capital as a percentage of sales is projected to be around the prior year level of 20.4%.

CAPITAL EXPENDITURE TO INCREASE TO A LEVEL OF AROUND € 900 MILLION

In 2018, capital expenditure is expected to be around € 900 million and thus above the prior year level (2017: € 752 million). Investments will mainly focus on controlled space initiatives of the adidas and Reebok brands, the company's IT and logistics infrastructure as well as the further development of the corporate headquarters in Herzogenaurach, Germany.

MANAGEMENT TO PROPOSE DIVIDEND OF € 2.60

As a result of the strong operational and financial performance in 2017, our strong financial position as well as Management's confidence in our short- and long-term growth aspirations, the adidas AG Executive and Supervisory Boards will recommend paying a dividend of € 2.60 per dividend-entitled share for 2017 (2016: € 2.00) to shareholders at the Annual General Meeting (AGM) on May 9, 2018. This represents a payout ratio of 37.1% (2016: 37.4%) based on the company's net income from continuing operations excluding the negative one-time tax impact in 2017. This is consistent with the prior year's payout ratio and in line with our long-term policy to distribute between 30% and 50% of net income from continuing operations to shareholders. [SEE OUR SHARE, P. 57](#)

RISK AND OPPORTUNITY REPORT

In order to remain competitive and ensure sustainable success, adidas consciously takes certain risks and continuously explores and develops opportunities. Our risk and opportunity management principles and system provide the framework for our company to conduct business in a well-controlled environment.

RISK AND OPPORTUNITY MANAGEMENT PRINCIPLES

We define risk as the potential occurrence of an external or internal event (or series of events) that may negatively impact our ability to achieve the company’s business objectives or financial goals. Opportunity is defined as the potential occurrence of an external or internal event (or series of events) that can positively impact the company’s ability to achieve its business objectives or financial goals. We have summarized risks in four main categories: Strategic, Operational, Legal and Compliance, and Financial. Opportunities are classified in two main categories: Strategic and Operational, and Financial.

RISK AND OPPORTUNITY MANAGEMENT SYSTEM

The Executive Board has overall responsibility for establishing an effective risk and opportunity management system that ensures comprehensive and consistent management of all material risks and opportunities. [SEE DIAGRAM 95](#) The Risk Management department governs, operates and develops the company’s risk and opportunity management system and is the owner of the centrally managed risk and opportunity management process on behalf of the Executive Board. The Supervisory Board is responsible for monitoring the effectiveness of the risk management system. These duties are undertaken by the Supervisory Board’s Audit Committee.

The Internal Audit department provides objective assurance to the Executive Board and Supervisory Board regarding the adequacy and effectiveness of the company’s risk and opportunity management system on a regular basis. In addition, the Internal Audit department includes an assessment of the effectiveness of risk management processes and compliance with the company’s Risk Management Policy as part of its regular auditing activities with selected adidas subsidiaries or functions each year.

To facilitate effective risk and opportunity management, we implemented a risk and opportunity management system, which is based on the integrated frameworks for enterprise risk management and internal controls developed and published by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Additionally, we have adapted our risk and opportunity management system to more appropriately reflect the structure as well as the corporate and management culture of the company. This

system focuses on the identification, evaluation, handling, monitoring and systematic reporting of risks and opportunities. The key objective of the risk and opportunity management system is to support business success and protect the company as a going concern through an opportunity-focused but risk-aware decision-making framework. Our Risk Management Policy outlines the principles, processes, tools, risk areas, key responsibilities, reporting requirements and communication timelines within our company.

Risk and opportunity management is a company-wide activity which utilizes key insights from the members of the Executive Board as well as from global and local business units and functions.

Our risk and opportunity management process comprises the following steps:

- **Risk and opportunity identification:** adidas continuously monitors the macroeconomic environment and developments in the sporting goods industry, as well as internal processes, to identify risks and opportunities as early as possible. Our company-wide network of Risk Owners (generally all leaders reporting directly to the Executive Board, including the Managing Directors of our markets) ensures an effective bottom-up identification of risks and opportunities. The Risk Management department has defined a catalog of potential risk areas (Risk Universe) to assist Risk Owners in identifying and categorizing risks and opportunities. The Risk Owners use various instruments in the risk and opportunity identification process, such as primary qualitative and quantitative research including trend scouting and consumer surveys as well as feedback from our business partners and controlled space network. These efforts are supported by global market research and competitor analysis. Through this process, we seek to identify the markets, categories, consumer target groups and product styles which show most potential for future

adidas risk and opportunity management system 95



growth at a local and global level. Equally, our analysis focuses on those areas that are at risk of saturation or exposed to increased competition or changing consumer tastes. However, our risk and opportunity identification process is not only limited to external risk factors or opportunities; it also includes an internal perspective that considers processes, projects, human resources and compliance aspects.

- **Risk and opportunity evaluation:** We evaluate identified risks and opportunities individually according to a systematic evaluation methodology, which allows adequate prioritization as well as allocation of resources. Risk and opportunity evaluation is also part of the Risk Owners' responsibility. The Risk Management department supports and guides the Risk Owners in the evaluation process.

According to our methodology, risks and opportunities are evaluated by looking at two dimensions: the potential impact and the likelihood that this impact materializes. Based on this evaluation, we classify risks and opportunities into five categories: marginal, minor, moderate, significant and major.

The potential impact is evaluated using five categories: very low, low, medium, high and very high. These categories represent quantitative or equivalent qualitative measurements. The quantitative measurements are based on the potential financial effect on the relevant income statement metrics (operating profit, financial result or tax expenses). Qualitative measurements used are, for example, the degree of media exposure or damage to people's health and safety. Likelihood represents the possibility that a given risk or opportunity may materialize with the specific impact. The likelihood of individual risks and opportunities is evaluated on a percentage scale divided into five categories: unlikely, possible, likely, very likely and almost certain. [SEE DIAGRAM 96](#)

Risk evaluation categories

Likelihood		Potential impact				
		Very low	Low	Medium	High	Very high
Almost certain	>85%				Material Risks	
Very likely	50%–85%					
Likely	30%–50%					
Possible	15%–30%					
Unlikely	<15%					
		Financial equivalent¹				
		≤ € 5 million	€ 5 million – € 20 million	€ 20 million – € 50 million	€ 50 million – € 100 million	≥ € 100 million
		Qualitative equivalent				
		Almost no media coverage	Limited local media coverage	Local and limited national media coverage	National and limited international media coverage	Extensive international media coverage
		Minor injuries to employees or third parties such as consumers, customers, vendors, athletes that do not require medical treatment.	Minor injuries to employees or third parties such as consumers, customers, vendors, athletes that require medical treatment.	Injuries to employees or third parties such as consumers, customers, vendors, athletes that lead to hospitalization.	Serious, life-changing injuries to employees or third parties such as consumers, customers, vendors, athletes.	Fatalities of employees or third parties such as consumers, customers, vendors, athletes.

Risk classification: ■ Marginal ■ Minor ■ Moderate ■ Significant ■ Major

¹ Based on operating profit, financial result or tax expenses.

When evaluating risks and opportunities, we also consider the earliest time period when the company's target achievement may be impacted, in order to provide a broad perspective and ensure early identification and mitigation. Short-term risks and opportunities may affect the achievement of the company's objectives already in the current financial year, mid-term risks and opportunities would impact the company's target achievement in the next financial year, while long-term risks and opportunities

might only have an effect on the achievement of the company's objectives after the next financial year.

We consider both gross and net risks in our risk assessments. While the gross risk reflects the inherent ('worst-case') risk before any mitigating action, the net risk reflects the residual ('expected') risk after all mitigating action. On the one hand, this approach allows for a good understanding of the impact of mitigating

action taken; on the other hand, it provides the basis for scenario analysis. Our assessment of risks presented in this report only reflects the net risk perspective. We measure the actual financial impact of the most relevant risks that materialized against the original assessment on a yearly basis. In this way, we ensure continuous monitoring of the accuracy of risk evaluations across the company, which enables us to continuously improve evaluation methodology based on our findings.

In assessing the potential effect from opportunities, each opportunity is appraised with respect to viability, commerciality and potential risks. This approach is applied to longer-term strategic prospects but also to shorter-term tactical and opportunistic initiatives at the corporate level as well as at the market and brand level. In contrast to the risk evaluation, only the net perspective exists for assessing opportunities.

- **Risk and opportunity handling:** Risks and opportunities are treated in accordance with the company's risk and opportunity management principles as described in the Risk Management Policy. Risk Owners are in charge of developing and implementing appropriate risk-mitigating action and exploiting opportunities within their area of responsibility. In addition, the Risk Owners need to determine a general risk-handling strategy for the identified risks, which is either risk avoidance, risk reduction with the objective to minimize impact and/or likelihood, risk transfer to a third party or risk acceptance. The decision on the implementation of the respective risk-handling strategy also takes into account the costs in relation to the effectiveness of any planned mitigating action if applicable. The Risk Management department works closely with the Risk Owners to monitor the continuous progress of planned mitigating action and assess the viability of already implemented mitigating action.

- **Risk and opportunity monitoring and reporting:** Our risk and opportunity management system aims to increase the transparency of risks and opportunities. As both risks and opportunities are subject to constant change, Risk Owners not only monitor developments but also the adequacy and effectiveness of the current risk-handling strategy on an ongoing basis.

Regular risk reporting takes place half-yearly and consists of a five-step reporting stream that is supported and facilitated by a globally used company-wide IT solution:

1. Risk Owners are required to report to Risk Management risks that have a possible gross impact of € 10 million and above or a net impact of € 1 million and above, both regardless of the likelihood of materializing. Risk Owners are also required to report all opportunities that have an impact of € 1 million and above.
2. Risk Management consolidates and aggregates the reported risks and opportunities and provides a consolidated report based on the Risk Owners' input to each member of the Executive Board concerning his or her individual area of responsibility. Each report specifically highlights substantial individual risks and opportunities. Each member of the Executive Board reviews the reported risks and opportunities of his or her individual area of responsibility, adding his or her own assessment of risks and opportunities if necessary.
3. Risk Management provides a consolidated report to all members of the Executive Board that includes both the assessment of each member of the Executive Board and the material risks and opportunities reported by Risk Owners. The Executive Board reviews the report, jointly agrees on a final company assessment of risks

and opportunities and decides if Risk Owners are required to take further action.

4. Based on the Executive Board's decision, Risk Management creates the final risk and opportunity report that is also shared with a selected group of leaders across the company.
5. The Executive Board in collaboration with Risk Management presents the final risk and opportunity assessment results to the Audit Committee of the Supervisory Board.

Material changes in previously reported risks and opportunities and/or newly identified risks and opportunities that are classified as moderate, significant or major as well as any issues identified which, due to their material nature, require immediate reporting, are also reported outside the regular half-yearly reporting stream on an ad hoc basis to the Risk Management department and the Executive Board.

COMPLIANCE MANAGEMENT SYSTEM (ADIDAS FAIR PLAY COMPLIANCE FRAMEWORK)

▣ We consider compliance with the law as well as with external and internal regulations to be imperative. Every employee is required to act ethically and in compliance with the law as well as with external and internal regulations while executing the company's business. Violations must be avoided under all circumstances. As a company with worldwide operations and more than 56,000 employees, however, we realize that it will never be possible to exclude compliance violations with absolute certainty.

The adidas Fair Play Compliance Framework and our risk and opportunity management system are closely aligned and both

are overseen by the company's Chief Compliance Officer who reports directly to the company's Chief Executive Officer. We see compliance as all-encompassing, spanning all business functions throughout the entire value chain, from supply chain through to the end consumer. In 2017, we therefore significantly increased the size of our central Compliance team and added dedicated regional Compliance teams based across our major regional hubs. The central Compliance team works closely with regional Compliance Managers and local Compliance Officers to conduct a systematic assessment of key compliance risks on a half-yearly basis. In addition, the central Compliance team regularly conducts detailed compliance risk assessments within selected entities.

The company's compliance management system is based on the OECD Principles of Corporate Governance. It refers to the OECD Guidelines for Multinational Enterprises and is designed to:

- Support the achievement of qualitative and sustainable growth through good corporate governance.
- Reduce and mitigate the risk of financial losses or damage caused by non-compliant conduct.
- Protect and further enhance the value and reputation of the company and its brands through compliant conduct.
- Preserve diversity by fighting harassment and discrimination.

Our Fair Play Code of Conduct, which is applicable globally and for all business areas, stipulates guidelines for behavior in everyday work, which all employees are obliged to comply with. The Code of Conduct is accessible on our website, on our intranet and as an app for smartphones. [ADIDAS-GROUP.COM/S/CODE-OF-CONDUCT](https://www.adidas-group.com/s/code-of-conduct) The Code of Conduct is the cornerstone of our compliance management program which is founded on three pillars: prevention, detection and response.

Prevention includes, for example, policies such as the company's Code of Conduct, the anti-bribery and corruption

policy, the privacy policy or the antitrust and competition law policy, training of employees or targeted compliance-related communication by management or the Compliance department. In 2017, more than 6,000 employees participated in our web-based Code of Conduct training, which is a mandatory component of employee onboarding, while around 2,700 employees completed our web-based anti-bribery and corruption training. In addition, 11,800 employees completed the Preventing Anti-Competitive Practices training. Furthermore, over 95% of senior executives were trained in dedicated three-hour compliance workshops and the members of the Executive Board also completed a separate compliance training session.

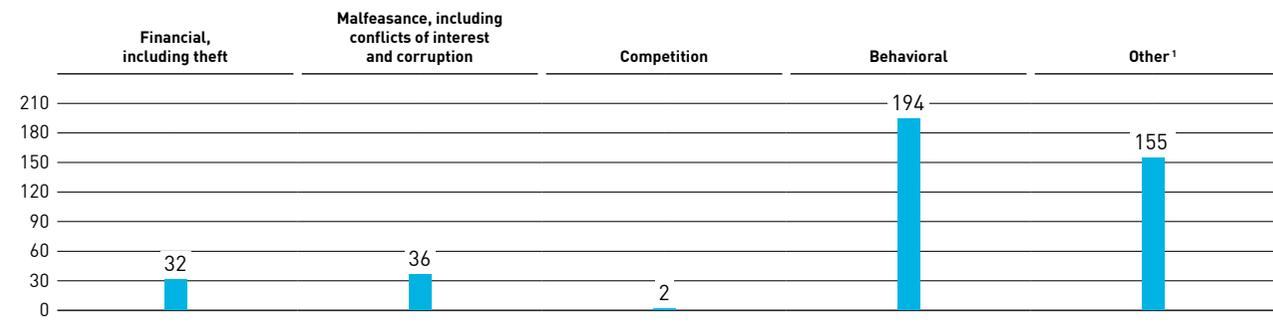
To ensure timely detection of potential infringements of statutory regulations or internal guidelines, we have implemented whistleblowing procedures which allow employees to either report concerns over wrongdoing/potential compliance violations internally (e.g. directly to their supervisor, to the Chief Compliance Officer, regional Compliance Managers or local Compliance Officers, the

relevant HR manager or the Works Council) or externally via an independent, confidential reporting hotline or email service. The hotline (named 'Fair Play hotline') is available at all times worldwide. In case of reported or suspected compliance violations, the Chief Compliance Officer or the Compliance department undertake the required investigations.

Appropriate and timely response to compliance violations is essential. Therefore, we have established a team of regional Compliance Managers and a global network of local Compliance Officers overseen by the Chief Compliance Officer as contact persons to whom complaints and information concerning compliance violations can be reported. We track, monitor and report potential incidents of non-compliance worldwide using a web-based reporting solution. In 2017, we recorded 419 potential compliance violations, representing a 26% increase compared to the prior year when 331 potential violations were recorded. [SEE DIAGRAM 97](#) [SEE DIAGRAM 98](#) This increase is attributable to ongoing senior management communication (e.g. reemphasizing our non-retaliation policy), training and workshops, which have led to improved

Potential compliance violations

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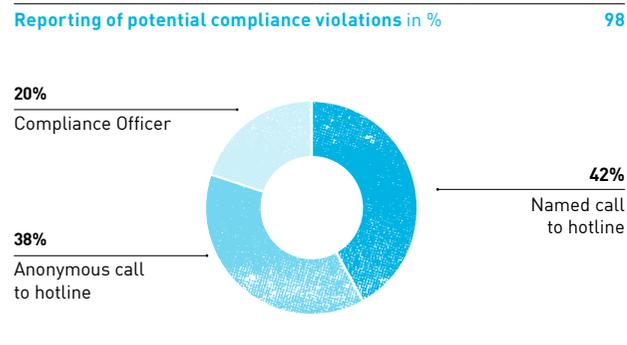


¹ Includes payroll issues, intellectual property and leaks of confidential information, inter alia.

employee awareness with respect to ethical conduct and our continuously improving compliance activities.

Appropriate sanction mechanisms, ranging from warnings through to termination of employment, are used to react promptly to confirmed compliance violations. Insights gained from the investigation of past violations are used to continuously improve the compliance management system.

Monthly key performance indicators, including those for participation in training and for compliance violations, are reported to the Executive Board by the Compliance department. The Chief Compliance Officer regularly reports to the Chief Executive Officer on the further development of the compliance program and on major compliance cases, which are also reported to the Audit Committee. Further, he reports to the Audit Committee at one of its meetings at least once a year concerning the contents and the further development of the compliance program. ▬



DESCRIPTION OF THE MAIN FEATURES OF THE INTERNAL CONTROL AND RISK MANAGEMENT SYSTEM RELATING TO THE CONSOLIDATED FINANCIAL REPORTING PROCESS PURSUANT TO § 315 SECTION 4 GERMAN COMMERCIAL CODE (HANDELSGESETZBUCH – HGB)

The internal control and risk management system relating to the consolidated financial reporting process of the company represents a process embedded within the company-wide corporate governance system. It aims to provide reasonable assurance regarding the reliability of the company's external financial reporting by ensuring company-wide compliance with statutory accounting regulations, in particular the International Financial Reporting Standards (IFRS) and internal consolidated financial reporting policies (Finance Manual). We regard the internal control and risk management system as a process based on the principle of segregation of duties, encompassing various sub-processes in the areas of Accounting, Controlling, Taxes, Treasury, Planning, Reporting and Legal, focusing on the identification, assessment, treatment, monitoring and reporting of financial reporting risks. Clearly defined responsibilities are assigned to each distinct sub-process. In a first step, the internal control and risk management system serves to identify and assess as well as to limit and control risks identified in the consolidated financial reporting process which might result in our consolidated financial statements not being compliant with internal and external regulations.

Internal Control over Financial Reporting (ICoFR) serves to provide reasonable assurance regarding the reliability of financial reporting and compliance with applicable laws and regulations despite identified financial reporting risks. To monitor the effectiveness of ICoFR, the Policies and Internal Controls department and the Internal Audit department regularly review accounting-related processes. Additionally, as part of the year-end audit, the external auditor selects and

examines internal controls, including IT controls, to assess their effectiveness. The Audit Committee of the Supervisory Board also monitors the effectiveness of ICoFR. However, due to the limitations of ICoFR, even with appropriate and functional systems absolute certainty about the effectiveness of ICoFR cannot be guaranteed.

All adidas companies are required to comply with the consolidated financial reporting policies (Finance Manual), which are available to all employees involved in the financial reporting process through the company-wide intranet. We update the Finance Manual on a regular basis, dependent on regulatory changes and internal developments. Changes to the Finance Manual are promptly communicated to all adidas companies. Clear policies serve to limit employees' scope of discretion with regard to recognition and valuation of assets and liabilities, thus reducing the risk of inconsistent accounting practices within the company. We aim to ensure compliance with the Finance Manual through continuous adherence to the four-eyes principle in accounting-related processes. In addition, each quarter, the local manager responsible for the accounting process within the respective company and the respective local Managing Director confirm adherence to the Finance Manual and to IFRS in a signed representation letter to the Accounting department.

The accounting for adidas companies is conducted either locally or by an adidas Shared Service Center. The majority of the IT Enterprise Resource Planning (ERP) systems used are based on a company-wide standardized SAP system. Some adidas companies use Navision-based ERP software. As part of an initiative aimed at harmonizing our system infrastructure (One ERP), we will also introduce an SAP-based ERP system within these adidas companies in the medium term. Following approval by the Finance Director of the respective adidas company, the local financial statements are transferred to a central consolidation system based on SAP SEM-BCS. At the

corporate level, the regularity and reliability of the financial statements prepared by adidas companies are reviewed by the Accounting and Controlling departments. These reviews include automated validations in the system as well as the creation of reports and analyses to ensure data integrity and adherence to the reporting logic. In addition, differences between current year and prior year financial data as well as budget figures are analyzed on a market level. If necessary, adidas seeks the opinion of independent experts to review business transactions that occur infrequently and on a non-

routine basis. After ensuring data plausibility, the centrally coordinated and monitored consolidation process begins, running automatically on SAP SEM-BCS. Controls within the individual consolidation steps, such as those relating to the consolidation of debt or of income and expenses, are conducted both manually and system-based, using automatically created consolidation logs. Any inadequacies are remedied manually by systematically processing the individual errors as well as differences and are reported back to the adidas companies. After finalization of all consolidation

steps, all items in the consolidated income statement and in the consolidated statement of financial position are analyzed with respect to trends and variances. Unless already otherwise clarified, the adidas companies are asked to explain any identified material deviations.

All financial systems used are protected against malpractice by means of appropriate authorization concepts, approval concepts and access restrictions. Access authorizations are reviewed on a regular basis and updated if required. The risk of data loss or outage of accounting-related IT systems is minimized through central control and monitoring of virtually all IT systems, centralized management of change processes and regular data backups.

Corporate risks overview

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	Potential impact	Change (2016 rating)	Likelihood	Change (2016 rating)
Strategic risks				
Risks related to distribution strategy	Very high	↑ (Medium)	Likely	
Consumer demand risks	Very high		Possible	
Risks related to technology change	High		Possible	
Competition risks	Medium		Likely	↑ (Possible)
Macroeconomic, sociopolitical and regulatory risks	Very high		Unlikely	
Operational risks				
Business partner risks	Very high	↑ (High)	Possible	
IT and cyber security risks	High		Possible	
Personnel risks	High		Unlikely	↓ (Possible)
Inventory risks	High		Unlikely	
Legal and compliance risks				
Data privacy risks	Very high		Possible	
Risks related to product counterfeiting and imitation	Very high		Possible	
Risks related to customs and tax regulations	High		Likely	
Fraud and corruption risks	Very high		Unlikely	
Financial risks				
Currency risks	Very high		Possible	↓ (Likely)
Credit risks	Very high	↑ (High)	Unlikely	
Interest rate and share price risks	Low		Possible	↓ (Likely)
Financing and liquidity risks	Very low		Very Likely	↑ (Likely)

ILLUSTRATION OF MATERIAL RISKS

This report includes an explanation of what we perceive as material risks to the achievement of the company's objectives in the time period from 2018 to 2020. Our presentation of risks in this year's Annual Report differs from the 2016 Annual Report as we have expanded our scope and do not only focus on risks that could impact the company's business performance over a one-year period. Besides our material risks, we also report the following risks that we deem to be relevant: competition risks, macroeconomic, sociopolitical and regulatory risks, personnel risks, inventory risks, fraud and corruption risks, credit risks, interest rate and share price risks as well as financing and liquidity risks. The risks overview table shows the assessment of all risks described below. [SEE TABLE 99](#)

STRATEGIC RISKS

Risks related to distribution strategy

The inability to appropriately influence the channels in which the company's products are sold constitutes a continuous risk. Gray market activity or parallel imports could negatively affect our own sales performance and the image of our

brands. Furthermore, changes to segmentation, store formats and channel strategies could lead to inadequate utilization of our multiple distribution channels as well as strong retaliation from our customers and franchise partners. An unbalanced portfolio of own-retail stores (e.g. overexposure to certain markets or store formats) or inappropriate store locations may result in worse-than-expected sales development and lower profitability. Failure to recognize and respond to consolidation in the retail industry could lead to increased dependency on particular retail partners, reduced bargaining power and, consequently, margin erosion. The inability to properly adjust our distribution strategy to the continuously changing retail industry, which is experiencing increasing substitution of physical retail stores by digital commerce platforms, could result in sales and profit shortfalls.

To mitigate these risks, adidas has developed and implemented clearly defined distribution policies and procedures to avoid overdistribution of products in a particular channel and limit the exposure to gray markets. We continuously monitor our own-retail store portfolio, which helps us identify imbalances and quickly take appropriate action such as store closure or remodeling. New store openings are managed according to a standardized company-wide business plan model, taking into account our many years of own-retail experience and best practices from around the world. In addition, we conduct specific training for our sales force to appropriately manage product distribution and ensure that the right product is sold at the right point of sale to the right consumer at an appropriate price. We invest significant resources in the further expansion of our own e-commerce activities and work closely with retail partners with strong expertise in digital commerce.

Consumer demand risks

Success in the sporting goods industry largely depends on the ability to anticipate and quickly respond to changes in

consumer demand or consumer trends. Consumer demand changes can be sudden and unexpected, particularly when it comes to fashion-related businesses. Therefore, failure to anticipate consumer demand, as well as creating and offering products that do not resonate with consumers, is a critical risk to the success of our brands. Because of average lead times of 12 to 18 months, we face a risk of short-term revenue loss in cases where we are unable to respond quickly to changes in consumer demand. Even more critical, however, is the risk of continuously overlooking new consumer trends or failing to acknowledge their potential magnitude over a sustained period of time.

To mitigate these risks, identifying and responding to shifts in consumer demand as early as possible is a key responsibility of our brand organizations and, in particular, of the respective Risk Owners. Therefore, we utilize extensive primary and secondary research tools as outlined in our risk and opportunity identification process. We continuously expand our consumer analytics efforts to read and quickly react to changes in demand or trend shifts. In addition, direct communication with consumers on social media platforms or direct touchpoints with consumers via our own e-commerce channel help us strengthen our understanding of consumer preferences and behavior and, as a result, help us to reduce our vulnerability to changes in demand. Through continuous monitoring of sell-through data and disciplined product lifecycle management, in particular for our major product franchises, we are able to better detect demand patterns and prevent overexposure.

Risks related to technology change

Technological advancement is happening at an unprecedented pace and has profound implications for our company's operations. Technologies such as 3D printing, augmented reality, blockchain and artificial intelligence are changing the way products and services are made, offered, experienced

and exchanged. Failure to anticipate, recognize and respond to changes in technology in a timely manner could disrupt the company's business model, lead to a deterioration of our competitive position in the marketplace and substantially affect our ability to achieve our strategic and financial goals.

In order to mitigate this risk, we established a cross-functional digital leadership group that identifies and assesses technology trends and coordinates adoption of new technologies. Furthermore, we build partnerships with technology and business leaders around the world to stay connected to the latest advancements. For example, we have entered into a partnership with Carbon, a Silicon Valley-based digital 3D manufacturing company. [SEE INNOVATION, P. 78](#)

Competition risks

Strategic alliances amongst competitors and/or retailers, the increase of retailers' own private label businesses and intense competition for consumers and promotion partnerships between well-established industry peers and new market entrants (e.g. new brands, *vertical retailers* [SEE GLOSSARY](#)) pose a substantial risk to adidas. This could lead to harmful competitive behavior, such as price wars in the marketplace or bidding wars for promotion partnerships. Sustained pricing pressure in key markets could threaten the company's financial performance and the competitiveness of our brands. Aggressive competitive practices could also drive increases in marketing costs and market share losses, thus hurting the company's profitability and market position. World leaders in digital technologies could threaten adidas' success in markets for sport, health and fitness apps.

To mitigate competition risks, we continuously monitor and analyze information on our competitors and markets in order to be able to anticipate unfavorable changes in the competitive environment rather than reacting to such changes. This enables us to proactively adjust our marketing and sales

activities when needed. Continuous investment in research and development ensures that we remain innovative and distinct from competitors. ■ [SEE INNOVATION, P. 78](#) We also pursue a strategy of entering into long-term agreements with key promotion partners such as FC Bayern Munich or Lionel Messi, as well as adding new partners to refresh and diversify our portfolio, e.g. Gabriel Jesus or Victoria Beckham. In addition, our product and communication initiatives are designed to increase brand desire, drive market share growth and strengthen our brands' market position.

Macroeconomic, sociopolitical and regulatory risks

Growth in the sporting goods industry is highly dependent on consumer spending and consumer confidence. Economic downturns and sociopolitical factors such as military conflicts, changes of government, civil unrest, nationalization or expropriation, in particular in regions where adidas is strongly represented, therefore could negatively impact the company's business activities and top- and bottom-line performance. In addition, substantial changes in the regulatory environment (e.g. trade restrictions, economic and political sanctions) could lead to potential sales shortfalls or cost increases. For example, the ongoing negotiations between the UK and the European Union regarding the UK's withdrawal from the European Union ('Brexit') could cause business and consumer uncertainty, create an additional administrative burden to adhere to changes in regulatory frameworks and also increase uncertainty concerning the future of the European Union.

To mitigate these macroeconomic, sociopolitical and regulatory risks, adidas strives to balance sales across key regions and also between developed and emerging markets. We also continuously monitor the macroeconomic, political and regulatory landscape in all our key markets to anticipate potential problem areas, so that we are able to quickly adjust our business activities accordingly upon any change in conditions. Potential adjustments may be a reallocation of

investments to alternative, more attractive markets, changes in product prices, closure of own-retail stores, more conservative product purchasing, tight working capital management and an increased focus on cost control. In addition, by building on our leading position within the sporting goods industry, we actively engage in supporting policymakers and regulators in their efforts to liberalize global trade and curtail trade barriers and also in order to proactively adapt to significant changes in the regulatory environment.

OPERATIONAL RISKS

Business partner risks

adidas interacts and enters into partnerships with various third parties, such as promotion partners, retail partners or suppliers. As a result, the company is exposed to a multitude of business partner risks.

Injuries to individual athletes or poor on-field performance on the part of sponsored teams or athletes could reduce their consumer appeal and eventually result in lower sales and diminished attractiveness of our brands. Failure to cement and maintain strong relationships with retailers could have substantial negative effects on our wholesale activities and thus the company's business performance. Losing important customers in key markets due to sub-par relationship management would result in significant sales shortfalls. We work with strategic partners in various areas of our business (e.g. product creation, manufacturing, research and development) or distributors in a few selected markets whose approach might differ from our own business practices and standards, which could also negatively impact the company's business performance and reputation. Similarly, failure to maintain strong relationships with suppliers or service providers could negatively impact the company's sales and profitability. Risks may also arise from a dependence on particular suppliers, customers or service providers.

Overreliance on a supplier for a substantial portion of the company's product volume, or overdependence on a particular customer, increases the company's vulnerability to delivery and sales shortfalls and could lead to significant margin pressure. Business partner default (including insolvency) or other disruptive events such as strikes may negatively affect the company's business activities and result in additional costs and liabilities as well as lower sales for the company. Unethical business practices or improper behavior on the part of business partners could have a negative spill-over effect on the company's reputation, lead to higher costs or liabilities and disrupt business activities.

To mitigate business partner risks, adidas has implemented various measures. For example, we generally include clauses in contractual agreements with athletes, clubs and federations or other promotion partners that allow us to suspend or even terminate our partnership in case of improper or unethical conduct. In addition, we work with a broad portfolio of promotion partners, including individual athletes, club teams and federations or associations in numerous sports in order to reduce the dependence on the success and popularity of a few individual partners. To ensure strong relationships with retailers, adidas is committed to delivering outstanding customer service and providing our retail partners with the support and tools required to establish and maintain a mutually successful business relationship. Customer relationship management is not only a key activity for our sales force but also of utmost importance to our company's top executives and second-line management. We also utilize a broad distribution strategy which includes further expansion of our direct-to-consumer business to reduce the risk of overreliance on particular key customers. Specifically, no single customer accounted for more than 5% of the company's sales in 2017. To reduce the risk of business interruption in the supply chain, we work with suppliers who demonstrate reliability, quality and innovation. Furthermore, in order to

minimize any potential negative consequences such as a violation of our Workplace Standards by our suppliers, we enforce strict control and inspection procedures at our suppliers and also demand adherence to social and environmental standards throughout our supply chain. ■ [SEE SUSTAINABILITY, P. 88](#) In addition, we have selectively bought insurance coverage for the risk of business interruptions caused by physical damage to suppliers' premises. To reduce dependency on any particular supplier, the company follows a strategy of diversification. In this context, adidas works with a broad network of suppliers and, for the vast majority of its products, does not have a *single-sourcing model* ■ [SEE GLOSSARY](#).

IT and cyber security risks

Theft or leakage of confidential and sensitive information or data (e.g. product data, employee data, consumer data) could lead to reputational damage, penalties and higher costs. Data leakage could trigger in-depth forensic investigation resulting in temporary unavailability of key systems and business interruption. Key business processes, including product marketing, order management, warehouse management, invoice processing, customer support and financial reporting, are all dependent on IT systems. A significant systems outage or application failure in our infrastructure or that of our business partners could therefore result in considerable disruptions to our business. Virus or malware attacks could also lead to systems disruption, result in the loss of business-critical and/or confidential information or harm data integrity.

To mitigate these risks, our IT organization proactively engages in system preventive maintenance, service continuity planning and adherence to applicable IT policies. Data security is managed by restricting user access based on job description and adhering to data protection regulations. We conduct security reviews of key systems and applications on a regular basis and have established monitoring and alert systems to detect and properly tackle IT security incidents. Additional

security measures such as anti-virus software and firewalls are designed to further protect our systems and critical information. We perform multiple backups at alternating data center locations for the company's core ERP system on a daily basis. In addition, for the ERP system, our contingency solution allows us to quickly switch to a remote site if necessary – without any loss of data. System security, controls and reliability are regularly reviewed and tested by the Internal Audit department. To increase awareness amongst employees with regard to information security and data privacy, we conduct various training programs and regular information campaigns.

Personnel risks

Achieving the company's strategic and financial objectives is highly dependent on our employees and their talents. In this respect, strong leadership and a performance-enhancing culture are critical to the company's success. Therefore, inconsistent or ineffective leadership as well as the failure to install and maintain a performance-oriented culture and ensure strong employee engagement amongst our workforce could also substantially impede our ability to achieve our goals. An ineffective, unbalanced allocation of resources to business activities could cause operational inefficiencies and result in lower employee engagement. In addition, global competition for highly qualified personnel remains fierce. As a result, the loss of key personnel in strategic positions and the inability to identify, recruit and retain sufficient numbers of highly qualified and skilled people who best meet the specific needs of our company pose substantial risks to our business performance. Unattractive or non-competitive management and employee remuneration may exacerbate these risks. In addition, a lack of sufficient training measures and inadequate documentation of critical know-how might dilute or lead to a loss of key capabilities.

Our People Strategy, aimed at fostering a corporate culture of confidence, creativity and collaboration that is needed to be

successful, is an essential part of our strategic business plan 'Creating the New' and is designed to reduce these risks.

■ [SEE PEOPLE AND CULTURE, P. 81](#) To optimize staffing levels and resource allocation (i.e. having the right people with the right skillsets in the right roles), we have launched a strategic workforce management initiative. We continuously invest in improving employer branding activities to be the 'employer of choice' in our industry and as a result attract and retain the right talent. We have also established a global recruiting organization to enhance our internal and external recruiting services and capabilities. In addition, we strengthen employee retention by providing employees with development and career opportunities (e.g. via our Talent Carousel program) and we focus on promoting from within the organization rather than recruiting externally. We also have attractive reward and incentive schemes in place, designed to further support long-term employee commitment.

Inventory risks

As we place initial production orders up to nine months in advance of delivery, adidas is exposed to inventory risks relating to misjudging consumer demand at the time of production planning. Overestimating demand could result in inappropriate capacity utilization at our suppliers' factories, lead to overproduction and cause excess inventory for the company as well as in the marketplace. This can have negative implications for our financial performance, including product returns, inventory obsolescence and higher levels of clearance activity as well as reduced liquidity due to higher operating working capital requirements. Similarly, underestimating demand can lead to product shortfalls at the point of sale. In this situation, adidas faces the risk of missed sales opportunities and/or customer and consumer disappointment, which could lead to a reduction in brand loyalty and hurt our reputation. In addition, the company faces potential profitability impacts from additional costs such as airfreight in efforts to speed up replenishment.

In order to mitigate these risks, we actively manage inventory levels, for example by continuous monitoring of stock levels as well as centralizing stock holding and clearance activities. We also continuously strive to improve our forecasting and material planning processes. [SEE INTERNAL MANAGEMENT SYSTEM, P. 102](#) In addition, our Global Operations function is continuously improving the agility and flexibility of our planning environment in order to shorten lead times and ensure availability of products while trying to avoid excess inventories. [SEE GLOBAL OPERATIONS, P. 74](#) In this context, the company's strategic priority 'Speed' is an important driver, leveraging market and sell-through data in new ways. This, in turn, enables us to respond quickly to consumer demand and to deliver concepts that are fresh and desirable and made available when and where they are wanted by the consumer. [SEE CORPORATE STRATEGY, P. 62](#)

LEGAL AND COMPLIANCE RISKS

Data privacy risks

As a globally operating company, adidas is subject to various laws and regulations concerning data protection and privacy. Non-compliance with such laws and regulations could lead to substantial penalties and fines. For example, non-compliance with the EU General Data Protection Regulation, which will be in force as of May 2018, may result in fines of up to 4% of annual net sales. In addition, publication of failure to comply with data protection and privacy regulations could cause significant reputational damage and result in a loss of consumer trust in our brands. As it is critical for the company's future success to constantly analyze and effectively utilize data, these risks have become increasingly important for the company.

To mitigate these risks, we have established a global data privacy policy that applies to all adidas businesses worldwide. In addition, our data protection officer and the data protection department are continuously monitoring the adherence to data privacy standards and provide training and guidance. We are also working with external partners and law firms to

ensure we understand legal requirements across the globe and take appropriate action to remain compliant.

Risks related to product counterfeiting and imitation

As popular consumer brands which largely rely on technological and design innovation, our brands are frequent targets for counterfeiting and imitation.

To reduce the loss of sales and the potential damage to brand reputation resulting from counterfeit products, the company makes use of extensive legal protection (generally through registration of trademarks) and works closely with law enforcement authorities, investigators and external legal counsel. Although we have stepped up measures such as product security labeling with our authorized suppliers, the development of these measures remains a key priority going forward.

Risks related to customs and tax regulations

Numerous laws and regulations regarding customs and taxes as well as changes in such laws and regulations affect the company's business practices worldwide. Non-compliance with regulations concerning product imports (including calculation of customs values), intercompany transactions or income taxes could lead to substantial financial penalties and additional costs as well as negative media coverage and therefore reputational damage, for example in case of understatements or underpayments of corporate income taxes or customs duties. Changes in regulations regarding customs and taxes may also have a substantial impact on the company's sourcing costs or income taxes. Therefore, we also create provisions in accordance with the relevant accounting regulations to account for potential disputes with customs or tax authorities.

To proactively manage such risks, we constantly seek expert advice from specialized law and tax advisory firms. We closely

monitor changes in legislation in order to properly adopt regulatory requirements regarding customs and taxes. In addition, our internal legal, customs or tax departments advise our operational management teams to ensure appropriate and compliant business practices. Furthermore, we work closely with customs authorities and governments worldwide to make sure we adhere to customs and import regulations and obtain the required clearance of products to fulfill sales demand.

Fraud and corruption risks

We face the risk that members of the Executive Board as well as our employees breach rules and standards that guide appropriate and responsible business behavior. This includes the risks of fraud, financial misstatements or manipulation, bribery and corruption.

Our Fair Play Compliance Framework helps us manage these risks in a proactive way and enables us to prevent, detect and adequately respond in case of fraudulent or corrupt behavior. Our Global Policy Manual provides a framework for basic work procedures and processes and our Fair Play Code of Conduct stipulates that every employee and our business partners shall act ethically in compliance with the laws and regulations of the legal systems where they conduct company business. In addition, our regional compliance managers and local compliance officers guide and advise our operating managers regarding fraud and corruption topics. Furthermore, we utilize controls such as segregation of duties in IT systems and data analytics technology to prevent or detect fraudulent activities.

FINANCIAL RISKS

Currency risks

Currency risks for adidas are a direct result of multi-currency cash flows within the company. Furthermore, translation impacts from the conversion of non-euro-denominated

results into the company's functional currency, the euro, might lead to a material negative impact on our company's financial performance. The biggest single driver behind this risk results from the mismatch of the currencies required for sourcing our products versus the denominations of our sales. The vast majority of our sourcing expenses are in US dollars, while sales are denominated in other currencies to a large extent – most notably the euro. Exposures are presented in the respective table. [SEE TABLE 100](#) The exposure from firm commitments and forecast transactions was calculated on a one-year basis.

In line with IFRS 7 requirements, we have calculated the impact on net income and shareholders' equity based on changes in our most important currency exchange rates. The calculated impacts mainly result from changes in the fair value of our hedging instruments. The analysis does not include effects that arise from the translation of our foreign entities' financial statements into the company's reporting currency, the euro. The sensitivity analysis is based on the net balance sheet exposure, including intercompany balances from monetary assets and liabilities denominated in foreign currencies. Moreover, all outstanding currency derivatives were re-evaluated using hypothetical foreign exchange rates to determine the effects on net income and equity. The analysis was performed on the same basis for both 2016 and 2017.

Based on this analysis, a 10% increase in the euro versus the US dollar at December 31, 2017 would have led to a € 7 million increase in net income. [SEE TABLE 101](#) The more negative market values of the US dollar hedges would have decreased shareholders' equity by € 255 million. A 10% weaker euro at December 31, 2017 would have led to a € 14 million decrease in net income. Shareholders' equity would have increased by € 334 million. The impacts of fluctuations of the US dollar against the Chinese renminbi and of the euro against the British pound and the Japanese yen on net income and

shareholders' equity are also included in accordance with IFRS requirements.

However, many other financial and operational variables that could potentially reduce the effect of currency fluctuations are excluded from the analysis. For instance:

- Interest rates, commodity prices and all other exchange rates are assumed constant.
- Exchange rates are assumed at a year-end value instead of the more relevant sales-weighted average figure, which we utilize internally to better reflect both the seasonality of our business and intra-year currency fluctuations.
- The underlying forecast cash flow exposure (which the hedge instrument mainly relates to) is not required to be revalued in this analysis.
- Operational issues, such as potential discounts for key accounts, which have high transparency regarding the

impacts of currency on our sourcing activities (due to their own private label sourcing efforts), are also excluded from this analysis.

Utilizing a centralized currency risk management system, we hedge currency needs for projected sourcing requirements on a rolling basis up to 24 months in advance. In rare instances, hedges are contracted beyond the 24-month horizon. [SEE TREASURY, P. 115](#) Our goal is to have the vast majority of our hedging volume secured six months prior to the start of a given season. The company also largely hedges balance sheet risks. Due to our strong global position, we are able to partly minimize currency risk by utilizing natural hedges. Our gross US dollar cash flow exposure calculated for 2018 was around € 6.0 billion at year-end 2017, which we hedged using forward exchange contracts, currency options and currency swaps. [SEE TABLE 100](#) Our Treasury Policy allows us to utilize hedging

Exposure to foreign exchange risk based on notional amounts € in millions

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	USD	GBP	JPY	CNY
As at December 31, 2017				
Exposure from firm commitments and forecast transactions	(5,824)	1,206	659	845
Balance sheet exposure including intercompany exposure	(154)	(17)	(6)	(43)
Total gross exposure	(5,978)	1,189	653	802
Hedged with other cash flows				
Hedged with currency options	453	(68)	(44)	
Hedged with forward contracts	4,465	(919)	(431)	(997)
Net exposure	(1,060)	202	178	(195)
As at December 31, 2016				
Exposure from firm commitments and forecasted transactions	(6,763)	985	615	252
Balance sheet exposure including intercompany exposure	(478)	(11)	(6)	28
Total gross exposure	(7,241)	974	609	280
Hedged with other cash flows	114			
Hedged with currency options	405		(54)	
Hedged with forward contracts	5,253	(985)	(578)	(53)
Net exposure	(1,469)	(11)	(23)	227

Sensitivity analysis of foreign exchange rate changes € in millions

101

	USD	GBP	JPY	CNY
As at December 31, 2017				
	EUR +10%	EUR +10%	EUR +10%	USD +10%
Equity	(255)	88	43	76
Net income	7	1	1	12
	EUR -10%	EUR -10%	EUR -10%	USD -10%
Equity	334	(101)	(52)	(76)
Net income	(14)	(3)	(1)	(11)
As at December 31, 2016				
	EUR +10%	EUR +10%	EUR +10%	USD +10%
Equity	(277)	85	53	48
Net income	7	1	1	7
	EUR -10%	EUR -10%	EUR -10%	USD -10%
Equity	355	(104)	(66)	(48)
Net income	(8)	(1)	(1)	(6)

instruments, such as currency options or option combinations, which provide protection from negative exchange rate fluctuations while – at the same time – retaining the potential to benefit from future favorable exchange rate developments in the financial markets.

Credit risks

A credit risk arises if a customer or other counterparty to a financial instrument fails to meet its contractual obligations. **SEE NOTE 30, P. 190** adidas is exposed to credit risks from its operating activities and from certain financing activities. Credit risks arise principally from accounts receivable and, to a lesser extent, from other third-party contractual financial obligations such as other financial assets, short-term bank deposits and derivative financial instruments. Without taking into account any collateral, the carrying amount of financial assets and accounts receivable represents the maximum exposure to credit risk.

At the end of 2017, there was no relevant concentration of credit risk by type of customer or geography. Our credit risk exposure is mainly influenced by individual customer characteristics. Under the company's credit policy, new customers are analyzed for creditworthiness before standard payment and delivery terms and conditions are offered. Tolerance limits for accounts receivable are also established for each customer. Both creditworthiness and accounts receivable limits are monitored on an ongoing basis. Customers that fail to meet the company's minimum creditworthiness are, in general, allowed to purchase products only on a prepayment basis.

Other activities to mitigate credit risks include retention of title clauses as well as, on a selective basis, credit insurance, the sale of accounts receivable without recourse, and bank guarantees.

Objective evidence that financial assets are impaired includes, for instance, significant financial difficulty of the issuer or debtor, indications of the potential bankruptcy of the borrower and the disappearance of an active market for a financial asset because of financial difficulties. The company utilizes allowance accounts for impairments that represent our estimate of incurred credit losses with respect to accounts receivable.

Allowance accounts are used as long as the company is satisfied that recovery of the amount due is possible. Once this is no longer the case, the amounts are considered irrecoverable and are directly written off against the financial asset. The allowance consists of two components:

- firstly, an allowance established for all receivables dependent on the aging structure of receivables past due date and
- secondly, a specific allowance that relates to individually assessed risks for each specific customer – irrespective of aging.

At the end of 2017, no customer accounted for more than 10% of accounts receivable.

The Treasury department arranges currency, commodity and interest rate hedges, and invests cash, with major banks of a high credit standing throughout the world. adidas subsidiaries are authorized to work with banks rated BBB+ or higher. Only in exceptional cases are subsidiaries authorized to work with banks rated lower than BBB+. **SEE TREASURY, P. 115** To limit risk in these cases, restrictions are clearly stipulated, such as maximum cash deposit levels. In addition, the credit default swap premiums of our partner banks are monitored on a monthly basis. In the event that the defined threshold is exceeded, credit balances are shifted to banks compliant with the limit.

We believe our risk concentration is limited due to the broad distribution of our investment business with more than 20 globally operating banks. At December 31, 2017, no bank accounted for more than 10% of our investments. Including subsidiaries' short-term deposits in local banks, the average concentration was 1%. This leads to a maximum exposure of € 98 million in the event of default of any single bank. We have further diversified our investment exposure by investing into AAA-rated money market funds.

In addition, in 2017, we held derivatives with a positive fair market value in the amount of € 101 million. The maximum exposure to any single bank resulting from these assets amounted to € 27 million and the average concentration was 4%.

In accordance with IFRS 7, the following table includes further information about set-off possibilities of derivative financial assets and liabilities. [SEE TABLE 102](#) The majority of agreements between financial institutions and adidas include a mutual right to set off. However, these agreements do not meet the criteria for offsetting in the statement of financial position, because the right to set off is enforceable only in the event of counterparty defaults.

The carrying amounts of recognized derivative financial instruments, which are subject to the mentioned agreements, are also presented in the following table. [SEE TABLE 102](#)

Set-off possibilities of derivative financial assets and liabilities € in millions **102**

	2017	2016
Assets		
Gross amounts of recognized financial assets	115	383
Financial instruments which qualify for set-off in the statement of financial position	0	0
Net amounts of financial assets presented in the statement of financial position	115	383
Set-off possible due to master agreements	(100)	(96)
Total net amount of financial assets	15	287
Liabilities		
Gross amounts of recognized financial liabilities	(280)	(112)
Financial instruments which qualify for set-off in the statement of financial position	0	0
Net amounts of financial liabilities presented in the statement of financial position	(280)	(112)
Set-off possible due to master agreements	100	96
Total net amount of financial liabilities	(180)	(16)

Interest rate and share price risks

Changes in global market interest rates affect future interest payments for variable-interest liabilities. As the company does not have material variable-interest liabilities, even a significant increase in interest rates should have only slight adverse effects on the company's profitability, liquidity and financial position. In addition, share price fluctuations may affect our Long-Term Incentive Plan (LTIP), which is a share-based remuneration scheme with cash settlement. In line with IFRS 7 requirements, we have calculated the impact on net income based on changes in the company's share price. A 10% increase in the adidas AG share price versus the closing share price at December 31, 2017 would have led to a € 5.8 million increase in net income whereas a 10% decrease in the adidas AG share price versus the closing share price at

December 31, 2017 would have led to a € 5.8 million decrease in net income.

To reduce interest rate risks and maintain financial flexibility, a core tenet of our company's financial strategy is to continue to use surplus cash flow from operations to reduce gross borrowings. Beyond that, we may consider adequate hedging strategies through interest rate derivatives in order to mitigate interest rate risks. [SEE TREASURY, P. 115](#) To reduce share price risks, the company uses derivative instruments to hedge against share price fluctuations.

Financing and liquidity risks

Liquidity risks arise from not having the necessary resources available to meet maturing liabilities with regard to timing, volume and currency structure. In addition, the company faces the risk of having to accept unfavorable financing terms due to liquidity restraints. Our Treasury department uses an efficient cash management system to manage liquidity risk. At December 31, 2017, cash and cash equivalents together with marketable securities amounted to € 1.604 billion (2016: € 1.515 billion). Moreover, our company maintains € 2.251 billion (2016: € 2.403 billion) in bilateral credit lines, which are designed to ensure sufficient liquidity at all times. Of these, € 600 million consist of core committed lines.

[SEE TREASURY, P. 115](#)

Future cash outflows arising from financial liabilities that are recognized in the consolidated statement of financial position are presented in the following table. [SEE TABLE 103](#) This includes payments to settle obligations from borrowings as well as cash outflows from cash-settled derivatives with negative market values. Financial liabilities that may be settled in advance without penalty are included on the basis of the earliest date of potential repayment. Cash flows for variable-interest liabilities are determined with reference to the conditions at the balance sheet date.

Future cash outflows € in millions

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	Up to 1 year	Up to 2 years	Up to 3 years	Up to 4 years	Up to 5 years	More than 5 years	Total
As at December 31, 2017							
Bank borrowings	106						106
Eurobond ¹	16	16	17	616	9	425	1,099
Accounts payable	1,975						1,975
Other financial liabilities	88	5					93
Accrued liabilities ²	837					1	838
Derivative financial liabilities	275	9					284
Total	3,297	31	17	616	9	426	4,395
As at December 31, 2016							
Bank borrowings	379						379
Eurobond ¹	16	16	16	17	616	435	1,116
Accounts payable	2,496						2,496
Other financial liabilities	90	16					107
Accrued liabilities ²	704	9					713
Derivative financial liabilities	110	3					113
Total	3,795	44	16	17	616	435	4,924

1 Including interest payments.

2 Accrued interest excluded.

We ended the year 2017 with net cash of € 484 million (2016: net borrowings of € 103 million).

ILLUSTRATION OF OPPORTUNITIES

In this report, we focus on opportunities we deem to be material for adidas in the period from 2018 to 2020. Our presentation of opportunities in this year's Annual Report differs from the 2016 Annual Report as we have expanded our scope and do not only focus on opportunities that could impact the company's business performance over a one-year period. The assessment is shown in the opportunities overview table.

SEE TABLE 104

STRATEGIC AND OPERATIONAL OPPORTUNITIES

Organic growth opportunities

Distribution strategy: The sporting goods retail environment is changing constantly. We therefore continue to adapt our distribution strategy to this constantly changing environment and have made controlled space initiatives a strategic priority. SEE CORPORATE STRATEGY, P. 62 This includes the further expansion of our own e-commerce activities, a clear focus on retail partners that provide consumers with the best shopping experience and customer service, retail space management with key retail partners, as well as the introduction and roll-out of new own-retail store formats. Successful results from

these initiatives could enable us to accelerate top- and bottom-line growth. SEE SALES AND DISTRIBUTION STRATEGY, P. 72

Partnerships: adidas is constantly evolving its partnership network within sport and culture, such as with academic organizations and companies from other industries in research and development. SEE INNOVATION, P. 78 These partnerships have generated multiple new growth opportunities for adidas, as we have acquired product or process know-how and gained access to new distribution channels or markets. Partnerships, strategic alliances and collaborations may enable us to pursue further growth and efficiency opportunities.

Product portfolio: Over the last years, we have benefited from strong consumer demand for selected product franchises such as UltraBOOST, Stan Smith or NMD. We believe that a continued focus on product franchises combined with disciplined product lifecycle management and well-executed distribution offers further upside potential both in terms of sales and profit. In addition, further optimizing pricing and range architecture could result in better-than-expected top-line growth and bottom-line improvements. We continue to see untapped sales potential at more commercial price points. Consequently, the further expansion in categories such as basketball and running, where we feel currently underrepresented, could result in additional market share and net sales growth and lead to further profitability improvements.

Opportunities related to organizational and process improvements

Data analytics: Data and analytics play a crucial role in enabling fact-based decision making. Therefore, we have established a dedicated Advanced Analytics team to drive business decision making by leveraging the power of data. Throughout 2018, we will continue to enhance our existing capabilities to build and scale insights-driven use cases, using latest technology that will bring value to our business

operations across the entire company. As a result, we could become faster and more efficient in our operations. We may increase visibility and understanding of consumer preferences, increase full-price sales, reduce discounts and optimize order book management, inventory management and purchasing. This could result in improved top- and bottom-line performance.

Process optimization: Continued optimization of key business processes and strict cost control are vital to achieving high profitability and return on invested capital. We are confident that there is still significant opportunity to improve process efficiency and effectiveness and further streamline cost structures throughout our company. Consequently, we will continue to focus on driving the standardization and harmonization of processes, as reflected by the company's 'ONE adidas' initiative. [SEE CORPORATE STRATEGY, P. 62](#) For example, further centralizing and bundling our global *non-trade procurement activities* [SEE GLOSSARY](#) could help realize additional cost savings. Our strategic workforce management initiative also not only mitigates the risk of unbalanced allocation of personnel across the company but could also

help us increase efficiency and productivity beyond our current expectations by optimizing organizational structures and capability management.

FINANCIAL OPPORTUNITIES

Favorable financial market changes

Favorable exchange and interest rate developments can potentially have a positive impact on the company's financial results. Our Treasury department closely monitors the financial markets to identify and exploit opportunities. Translation effects from the conversion of non-euro-denominated results into our company's functional currency, the euro, might positively impact our company's financial performance. [SEE TREASURY, P. 115](#)

Corporate opportunities overview

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	Potential impact	Change (2016 rating)	Likelihood	Change (2016 rating)
Strategic and operational opportunities				
Organic growth opportunities	Very high	↑ (High)	Possible	
Opportunities related to organizational and process improvements	High	↑ (Medium)	Likely	↑ (Possible)
Financial opportunities				
Favorable financial market changes	Very high		Possible	

MANAGEMENT ASSESSMENT OF PERFORMANCE, RISKS AND OPPORTUNITIES, AND OUTLOOK

ASSESSMENT OF PERFORMANCE VERSUS TARGETS

We communicate our financial targets on an annual basis. We also provide updates throughout the year as appropriate. In 2017, the company delivered a strong operational and financial performance. Sales development was favorably impacted by rising consumer spending on sporting goods, supported by global trends such as increasing penetration of sportswear ('athleisure'), increasing health awareness and rising sports participation rates. [SEE ECONOMIC AND SECTOR DEVELOPMENT, P. 105](#) The strong brand momentum, supported by innovative product launches and inspiring marketing campaigns, as well as the successful execution of the company's strategic business plan 'Creating the New' drove strong sales and earnings growth throughout the year. As a result, we increased our full-year top- and bottom-line guidance in July 2017. [SEE TABLE 105](#)

In 2017, revenues increased 16% on a currency-neutral basis, driven by double-digit growth at the adidas brand. Currency-neutral sales grew at double-digit rates in nearly all market segments. As a result, revenues increased above our initial guidance of 12% to 14% currency-neutral sales growth. Gross margin increased 1.2 percentage points to 50.4%, exceeding our initial forecast of an increase of up to 0.3 percentage points. This development was due to the larger-than-expected positive effects from a better pricing and product mix, which more than offset headwinds from unfavorable currency movements. The operating margin increased 1.2 percentage points to a level of 9.8%, which was above our initial guidance of an increase of between 0.2 and 0.4 percentage points. This development was

due to the gross margin increase as well as the positive effect from lower other operating expenses as a percentage of sales, which more than offset the decline in other operating income. As a result, net income from continuing operations, excluding the negative one-time tax impact in 2017, was up 32% to € 1.430 billion, and thus exceeded our initial guidance of an improvement at a rate between 13% and 15%. [SEE INCOME STATEMENT, P. 107](#)

In 2017, average operating working capital as a percentage of sales ended the year at a level of 20.4%. This development represents a decrease compared to the prior year level of 21.1%, while our initial guidance was for a modest increase. Capital expenditure (excluding acquisitions) amounted to € 752 million in 2017, below our initial guidance of around € 1.1 billion, mainly reflecting fewer-than-expected store openings throughout the year. Investments were mainly focused on controlled space initiatives of the adidas and Reebok brands, aimed at further strengthening our own-retail activities, franchise store presence and shop-in-shop presentations. Other areas of investment included logistics infrastructure and IT systems as well as the further development of our corporate headquarters in Herzogenaurach, Germany. [SEE STATEMENT OF FINANCIAL POSITION AND STATEMENT OF CASH FLOWS, P. 111](#)

Beyond our financial performance, we also actively monitor non-financial KPIs. [SEE INTERNAL MANAGEMENT SYSTEM, P. 102](#) In 2017, our Net Promoter Score (NPS) saw further improvements, reflecting the strong momentum of our brands and products throughout the year. [SEE PEOPLE AND CULTURE, P. 81](#) Also from a market share perspective, we continue to be very encouraged by our strong performance in key categories and key markets, as defined in the company's strategic business plan. North America and Greater China, two of our focus markets, were once again notable standouts, as we were able to further improve our market share in these regions. [SEE GLOBAL OPERATIONS, P. 74](#) Our diligence and discipline in sustainability matters continues to yield strong recognition

for our company. In 2017, adidas AG was again represented in a variety of high-profile sustainability indices. For the 18th consecutive time, adidas AG was selected to join the Dow Jones Sustainability Indices (DJSI), the world's first global sustainability index family tracking the performance of the leading sustainability-driven companies worldwide. In the sector 'Textiles, Apparel & Luxury Goods', we were rated industry best in the criteria Human Rights, Supply Chain Management, Impact Measurement and Valuation, Materiality, Environmental Policy and Management Systems, Risk and Crisis Management, Brand Management, Corporate Citizenship and Philanthropy, and Customer Relationship Management. [SEE SUSTAINABILITY, P. 88](#) As we are convinced that our employees' feedback plays a crucial role in our pursuit of creating a world-class work environment, during the course of 2017, we kicked off a new approach and system platform ('People Pulse') for a monthly measurement of the level of employee satisfaction. Following the implementation of this approach in June 2017, our monthly participation rates toward year-end exceeded our minimum participation rate target. In 2018, we aim to further expand People Pulse across the organization and build on the key learnings from the surveys. [SEE PEOPLE AND CULTURE, P. 81](#) Finally, we continue to enjoy a strong level of on-time in-full (OTIF) deliveries to our customers and own-retail stores. In 2017, OTIF saw a slight improvement compared to the prior year level and we are well on track to achieve our mid-term target. [SEE GLOBAL OPERATIONS, P. 74](#)

ASSESSMENT OF OVERALL RISKS AND OPPORTUNITIES

Our Risk Management team aggregates all risks and opportunities reported by Risk Owners and Executive Board members through the half-yearly risk and opportunity assessment process. Results from this process are analyzed and reported to the Executive Board accordingly. In addition, the Executive Board discusses and assesses risks and opportunities on a regular basis. [SEE RISK AND OPPORTUNITY REPORT, P. 131](#)

Taking into account the potential financial impact as well as the likelihood of materializing of the risks explained within this report, and considering the strong balance sheet as well as the current business outlook, we do not foresee any material jeopardy to the viability of the company as a going concern. This assessment is also supported by the historical response to our financing demands. adidas therefore has not sought an official rating by any of the leading rating agencies. We remain confident that our earnings strength

forms a solid basis for our future business development and provides the resources necessary to pursue the opportunities available to the company. Compared to the prior year, our assessment of certain risks has changed in terms of likelihood of occurrence and/or potential financial impact. The partial changes in risk evaluation have no substantial impact on the overall adidas risk profile, which we believe remains unchanged compared to the prior year.

ASSESSMENT OF FINANCIAL OUTLOOK

In March 2015, adidas unveiled 'Creating the New', its 2020 strategic business plan, which defines strategic priorities and objectives for the period up to 2020. The strategy is designed to drive brand desirability which, in turn, is expected to spur top- and bottom-line growth for the company in the years to come. Our successes since 2016, as measured by financial as well as non-financial KPIs, are a direct consequence of relentlessly executing Creating the New. Therefore, we will continue to focus on further executing against our strategic business plan, while at the same time fine-tuning it wherever needed and whenever necessary.

In March 2017, Creating the New was updated with complementary initiatives in order to grow the top and bottom line even faster than initially projected. This will ensure we continue our momentum in the years to come, resulting in strong sales and profitability improvements until 2020. Consequently, we increased our financial targets for 2020. We project currency-neutral revenues to increase at a rate of 10% to 12% on average per year until 2020 compared to the 2015 results. By outperforming the sporting goods industry, our brands will increase market share over the period. This, in combination with the expected gross margin improvement and our ability to generate operating leverage, will significantly increase our profitability. As a result, net income from continuing operations is expected to grow at a higher rate than the top line. While in March 2017, we projected net

Company targets versus actual key metrics

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	2016 Results ¹	2017 Initial targets ^{1,2}	2017 Updated targets ^{1,3}	2017 Results ¹	2018 Outlook
Sales (year-over-year change, currency-neutral)	20%	to increase at a rate between 12% and 14%	to increase at a rate between 17% and 19%	16%	to increase at a rate around 10%
Gross margin	49.2%	to increase up to 0.3pp	to increase up to 0.8pp	50.4% 1.2pp	to increase up to 0.3pp to a level of up to 50.7%
Other operating expenses (in % of net sales)	42.7%	below prior year level	below prior year level	41.9% (0.8pp)	below prior year level
Operating profit (€ in millions)	1,582	to increase at a rate between 13% and 15%	to increase at a rate between 24% and 26%	2,070 31%	to increase at a rate between 9% and 13%
Operating margin	8.6%	to increase between 0.2pp and 0.4pp	to increase up to 0.6pp	9.8% 1.2pp	to increase between 0.5pp and 0.7pp to a level between 10.3% and 10.5%
Net income from continuing operations ⁴ (€ in millions)	1,082	to increase at a rate between 13% and 15%	to increase at a rate between 26% and 28%	1,430 32%	to increase at a rate between 13% and 17% to a level between € 1.615 billion and € 1.675 billion
Basic earnings per share from continuing operations ⁴ (in €)	5.39	to increase at a rate between 13% and 15%	to increase at a rate between 25% and 27%	7.05 31%	to increase at a rate between 12% and 16%
Average operating working capital (in % of net sales)	21.1%	modest increase	modest increase	20.4% (0.7pp)	around prior year level
Capital expenditure ⁵ (€ in millions)	642	around € 1.1 billion	up to € 1.0 billion	752 17%	to increase to a level of around € 900 million

¹ Figures reflect continuing operations as a result of the divestiture of the Rockport, TaylorMade, Adams Golf, Ashworth and CCM Hockey businesses.

² As published on March 8, 2017.

³ As published on July 27, 2017.

⁴ 2017 excluding negative one-time tax impact of € 76 million.

⁵ Excluding acquisitions and finance leases.

income from continuing operations to expand by 20% to 22% on average per year during the five-year period, we now expect net income from continuing operations to grow by 22% to 24% on average per year, following the strong operational and financial performance in 2017. ■ [SEE CORPORATE STRATEGY, P. 62](#)

Through our extensive pipeline of new product launches paired with brand-building activities, the positive effects from major sporting events, including the 2018 FIFA World Cup, as well as through tight control of inventory levels and stringent cost management, we project strong revenue and profitability improvements in 2018. Our net income is expected to benefit from a further expansion in gross margin and the positive effect of lower other operating expenses as a percentage of sales. ■ [SEE SUBSEQUENT EVENTS AND OUTLOOK, P. 128](#) We believe that our outlook for 2018 is realistic within the scope of the current trading and economic environment.

Assuming no significant deterioration in the global economy, we are confident that we will achieve strong top- and bottom line improvements in 2018. However, ongoing uncertainties regarding the economic outlook and consumer sentiment in both developed and emerging economies as well as persisting high levels of currency volatility represent risks to the achievement of our stated financial goals and aspirations. ■ [SEE ECONOMIC AND SECTOR DEVELOPMENT, P. 105](#) No other material event between the end of 2017 and the publication of this report has altered our view.