

**ANNUAL  
REPORT**



# 02

# GROUP MANAGEMENT REPORT

OUR COMPANY

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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.

## 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. [SEE DIAGRAM 21](#)

### 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.

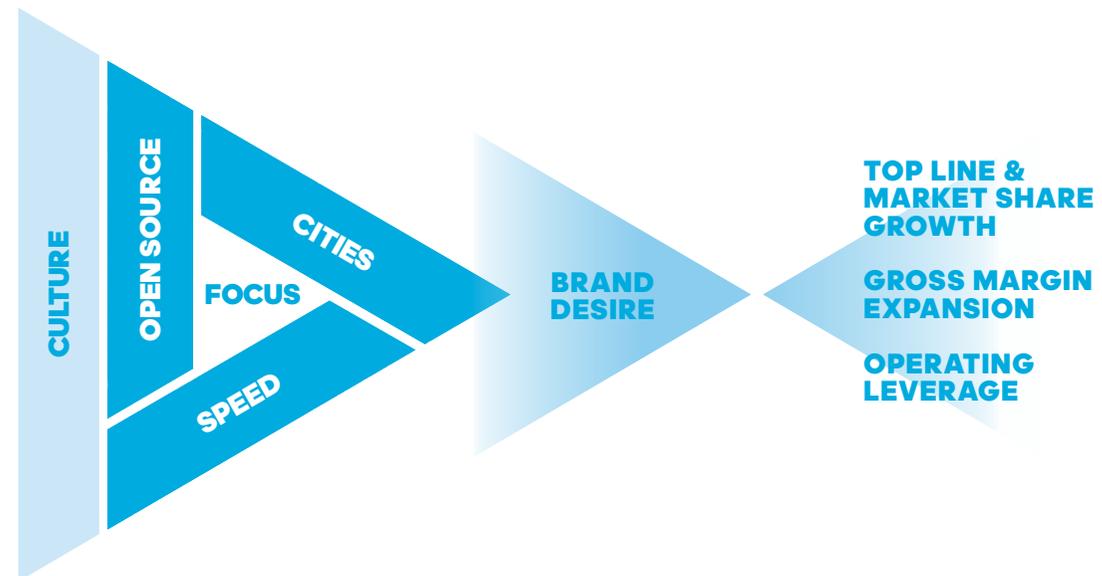
### Culture

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. In addition, the Global High Potential Group was formed in 2018 to identify and develop high potentials who have the ability to take on more complex, demanding and higher-level responsibilities at a global senior management level.

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, was simplified and linked to the development of the company's bottom line and our share price 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. We have made further progress in this regard. Karen Parkin was appointed to the Executive Board already in May 2017. In addition, the share of women in leadership positions across the company increased to 33% in 2018 compared to 29% in 2015.

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 fulfill higher consumer demand than initially forecasted.
- **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 37% in 2018,

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, Speedfactory allows the production process to become faster, leading to reduced lead times. Accelerated speed to market and the Speedfactories' proximity to consumers helps us to respond more quickly to trends and shifts in the marketplace, which ultimately enables adidas to satisfy consumers' expectations with greater speed and precision. 2018 saw the introduction of new *high-performance products* SEE GLOSSARY manufactured in our Speedfactories: The AM4 cities series, individually designed and manufactured shoes made for our six global key cities, as well as additional limited editions specific to cultural and sporting moments, such as the Stanley Cup victory of the Washington Capitals, were introduced. 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. Major successes in 2018 include the '747 Warehouse' around the NBA All-Star weekend in Los Angeles, where we offered cross-category product installations and created an unprecedented experience with creativity, sport and culture for the local community and over 20,000 visitors. We also launched 'Republic of Sports' in Shanghai, where 60,000 creators interacted with us through sports activities, Maker Lab and Parley experiences. In addition, the '/// <3 NYC (adidas loves New York)' campaign in New York created brand heat through a series of community-focused activations.
- **Products:** We continue to drive a multi-pronged strategy of product introductions, focused across all six cities, including global campaign launches and exclusive collections. After the initial 2017 launch of the AM4 series produced in our Speedfactory, we expanded the collection to Tokyo, Shanghai, Los Angeles and New York. We also introduced key technologies, for instance, the launch of Alphaedge 4D exclusively in our global key cities.

- **Experiences:** We are committed to providing premium retail experiences to our consumers with executions that connect, engage and inspire them. The opening of our largest Asia-Pacific Brand Center NJE800 in Shanghai showcased the latest retail concepts and innovations from adidas. The Brand Center features products from all categories and provides a multi-functional training venue, a 'Protect the Oceans' themed Run Lab, and a Creator Lab for customized services. Integrating retail concepts with sports experiences into one sports hall, the new Brand Center provides a space where sports enthusiasts can explore the latest trends and make the most of their creativity. Moreover, in collaboration with our retail partners, we continue to execute our strategy in key trade zones to transform our retail spaces into premium shopping destinations.

The 2018 results for specific 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. Last year, we continued to experience an improvement in brand desire which helped us to extend our market share in 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. In collaboration with the Brooklyn Creator Farm – a design space and creation hub we offer for urban creative talent, where we invite them to fuel innovation in sport with their ideas – we launched our first-ever laceless basketball silhouette N3XT L3V3L with the new Lightstrike midsole, Marquee BOOST, a lightweight model inspired by past designs, and the Pro Vision featuring a Bounce midsole. In addition, we continued our successful creative partnerships with Alexander Wang, Kanye West, Pharrell Williams, and Stella McCartney, among others, to drive brand desire and growth globally.
- **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 efforts in digital and physical spaces. For instance, in 2018 our 'adidas Runners' communities accounted for 180,000 active runners in 50 cities. And driven by our adidas Runners communities, close to one million runners got involved in the 'Run for the Oceans' campaign with around 200 events taking place in over 60 countries. In total, participants collected over 12 million kilometers and tracked their runs on Runtastic (and Joyrun for those based in China).
- **Partner collaborations:** The strategic initiatives in this area 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. We keep working with Parley to prevent plastic from entering our oceans and transform it into high-performance sportswear. In 2018, we expanded the sustainability efforts with new silhouettes such as Deerrupt, and with a new collection of outdoor footwear and apparel. We have recycled up to 1,000 tons of plastic per year with Parley and produced more than five million pairs of shoes using *Parley Ocean Plastic* [SEE GLOSSARY](#) in 2018. [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. In 2018, the Futurecraft 4D was launched and all product drops were sold out within 24 hours. [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 want to grow the numbers of users in our digital ecosystem. We have made significant progress in this regard and are now connected with more than 500 million users through our different platforms and social media channels. With the insights generated through Open Source, we craft better products and services for our consumers, driving 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. After the completion of the sale of the TaylorMade, Adams Golf and Ashworth brands as well as our CCM Hockey business in 2017, we are now operating with a narrowed focus on 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 2018, we continued to execute upon Reebok's turnaround plan 'Muscle Up', aimed at accelerating the brand's top-line growth in the US 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 four years, despite a 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 2018.

#### 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. After having successfully operationalized the initiatives under the *Brand Leadership* [SEE GLOSSARY](#) pillar in 2018, we are now focusing on the remaining two pillars – marketing effectiveness and operating efficiency. 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, 2018 saw the continuation of several initiatives kicked off in 2017 which are aimed at significantly improving our operating efficiency and profitability in the years to come. Our disciplined execution has already led to initial positive results. For example, our *Non-Trade Procurement* [SEE GLOSSARY](#) initiative, which is focused on enabling more efficient sourcing of goods and services not linked to the products sold to the consumer, started to deliver sustainable savings through the application of latest procurement practices and technologies such as e-auctions, e-catalogs and e-marketplaces. We decided to use these benefits to reinvest into the business and continue our investment efforts into our scalable business model. In

addition, with the roll-out and expansion of our Global Business Services in 2018, we continue to work on the standardization and harmonization of processes in areas such as Accounting and HR Services. These and other initiatives are designed to enable scalability and operating leverage 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 2018, we made good progress with multiple digital accelerators. After the initial launch in 2017, we rolled out our adidas App to a further 23 countries. As a result, by the end of 2018, our adidas App was live in 25 countries, with more than seven million downloads. Furthermore, we launched Creators Club in the US and Japan. With this membership program, we provide our consumers with personalized content and offerings, easy access to products and events, exclusive offers and promotions, recognitions and rewards, as well as an integrated experience with our sustainability programs. By providing consumers with a premium, connected and personalized shopping experience, we are on the right track to reach our 2020 own e-commerce revenue target of € 4 billion. In 2018, our own e-commerce platform was our fastest-growing channel with a currency-neutral revenue increase of 36%. In addition, we are developing our enterprise-level digitalization capabilities, such as end-to-end Digital Creation, with the goal of digitizing the entire value chain from product creation to point of sale.

### 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. 103](#)

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 of 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. Our dividend policy is complemented by a multi-year share buyback program announced in March 2018. Under the current program, we plan to buy back own shares for up to € 3 billion in total until May 2021, of which € 1 billion was utilized in 2018.

## 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 and in a sustainable way.

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 2018, we created a new Advanced Concepts team across the Sport Performance business units. The purpose of this team is to lead, control and manage the adidas innovation pipeline in order to service and deliver superior concepts to the different categories. This will allow the Future team to focus on larger upstream innovation with the intent and focus being to create new brand platforms and extensions of existing platforms. Furthermore, we created a vertically integrated Outdoor organization. This will enable us to incubate the Outdoor business, test new business models and nurture new business opportunities. Vertical integration and co-location will allow the Outdoor team to operate in a start-up manner, make quick decisions and drive clear accountability across all functions.
- **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.

- **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. 103](#)

### PRODUCT FRANCHISES: CREATE THE MOST DESIRED SYMBOLS OF SPORT IN THE WORLD

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 design, 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 2018, key adidas brand footwear franchises included UltraBOOST, PureBOOST, Alphabounce, Predator, and NMD. On the apparel side, we continued to build out franchises on the success of the Z.N.E. Hoodie and Tiro Pant.

## WOMEN'S: A NEW DIMENSION TO DRIVE GROWTH

Winning the female consumer continues to be a key focus as it offers one of the largest business opportunities for the adidas brand, with the women's category leading the growth in the sportswear industry. In 2018, the adidas brand further invested resources in expanding a cross-functional women's organization and support infrastructure to set direction for creative, ranging, merchandising and marketing as well as to steer cross-category planning. When it comes to winning the female consumer, adidas has focused its initiatives across product, retail, and activation. Highlights from these initiatives include:

- **Product:** adidas has been investing in key product areas that are critical to winning the trust of the female consumer, including bras, tights and running footwear, as well as improving overall apparel fit for the female consumer. In 2018, adidas introduced new bras and tights with positive response from both consumers and testers. adidas has also invested in research around the vertical female athlete, that will enable the future creation of products that will help her improve her game.
- **Retail:** adidas has taken steps toward enhanced merchandising and storytelling across our brand, building off female consumer shopping insights, to enable a seamless shopping experience for her to mix and match product. adidas has also rolled out a bra fitting training program in adidas own-retail stores, covering more than 500 own-retail doors with continued investment planned, ensuring the floor staff is upskilled in bra fitting services to better support our customers in finding the right product.

- **Activation:** One of the cornerstones of the adidas Women's approach continues to be the Creator Network. Powered by sport, fueled by culture, and fostered by collaboration, the Creator Network is a collective of athletes, influencers and innovators such as Karlie Kloss, Hannah Bronfman and Robin Arzon. Additionally, adidas has invested in female communities in key cities across the world, creating a direct relationship with the female consumer to collaborate with her, gather product feedback, gain insight on future opportunities and understand the barriers to sport she faces. A key highlight in this regard was the launch of a new purpose-driven platform at the US Open in New York in August 2018 focused on removing obstacles to sport for girls and elevating the conversation around equality in sport across genders.

## 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 marketing investments going forward. While the brand historically spent 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:** This 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, the Olympic Games, and the Boston and Berlin Marathons.
- **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 and Damian Lillard, 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 and Alexander Wang. In 2018, we added new collaborators such as Childish Gambino and Jonah Hill.

## 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 2018, we activated close to a million runners across the world to raise funds and awareness for the fight against ocean plastic through the Run For The Oceans. We created more than five million pairs of shoes using Parley Ocean Plastic, alongside two million pieces of apparel, and restated our ambition to reduce the use of virgin plastic.

[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 three overarching roles: Lead, Grow, 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 investing in the brand's football footwear franchises. In 2018, the adidas brand implemented innovations in its football footwear business with the continued focus on the Predator, 'X' and Nemeziz franchises as well as re-launching the most iconic football boot of all time – Copa. Leveraging the FIFA World Cup, the biggest event in sport, adidas achieved its objective of being the most influential brand during the event via its most personal campaign ever. The brand campaign featured a launch film with more than 50 assets and a global call to action for consumers to co-create content. The campaign drove reach, achieving the highest engagement rate for adidas in 2018.

— 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. In 2018, we incubated new concepts and achieved a greater balance between our classic models and new and innovative concepts. We have also incorporated more technology innovation such as BOOST or Carbon 4D into Originals products. At the same time, we continued to proactively manage the life cycles of our iconic franchises – Superstar and Stan Smith – to ensure healthy sell-through and inventory levels.

### Grow

— The running category is the adidas brand's biggest growth opportunity across all genders and price points. 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. The adidas brand, for example, has introduced groundbreaking innovation in materials such as BOOST and pioneering new manufacturing processes driven through Speedfactory. To spur growth, amongst other things, adidas Running will significantly

refine and evolve its franchise strategy for the male and female athlete across price points, increase its investment in running communities and grassroots activations through the adidas Runners communities in over 100 cities around the world, as well as play a central role in driving the future of digital in sport in cooperation with Runtastic. Running will also continue to play a major part in our sustainability strategy through the Run For The Oceans activation.

— 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](#)

— 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.

### 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, rugby, tennis, 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, Reebok has gone through a transformation from traditional sports to the sport of fitness. On this journey, Reebok has invested in its newly established 'Sport' unit 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. 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. Rooted in Reebok's heritage, the

brand is putting women at the heart of everything. This female-centric approach, with women being the focal point of content strategy, product creation, 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 2018, Reebok successfully launched the PureMove Bra, a revolutionary sports bra featuring patented fabric technology that adapts to movement and intensity. This product was then featured in a women's-only brand campaign.

### PRODUCT FRANCHISES: LEVERAGING THE BRAND'S FITNESS DNA

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

For this reason, Reebok continues to heavily invest in franchises, making them a key priority. By 2020, Reebok expects key apparel franchises to represent at least 25% of the brand's total apparel business. Key franchises include *performance products* [SEE GLOSSARY](#) such as the Lux Tight or Epic Short. The newest franchise, the PureMove Bra, won several coveted awards in 2018, including TIME's Best Inventions of 2018.

In footwear, Reebok continues to grow franchises that have been authenticated by their respective communities, such as the CrossFit Nano and the FloatRide Run. In 2018, the FloatRide Run Fast, an iteration of the running franchise, won the prestigious Runner's World Gear of the Year award. In addition, Reebok leverages its unique fitness DNA through iconic styles such as the Aztrek, the Classic Leather and the Club C.

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, 2019 will see continued storytelling around the Sole Fury, footwear built with a distinct split cushioning outsole, removing excess weight for 360-degree breathability and lightweight cushioning. Beyond technology platforms, Reebok remains committed to investing into innovation that consumers can relate to, fostered by unique collaborations and stories. [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 several relevant assets and influencers in the digital ecosystem.

— **Be More Human:** Inspiring people to be their absolute best selves 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. With the latest evolution, Reebok celebrated strong women who have made positive changes to the world in unique ways. The campaign featured some of the world's most respected athletes and sought-after artists, including Katrin Davidsdottir, Danai Gurira, Gigi Hadid, Ariana Grande and Nathalie Emmanuel. These women told their personal stories about overcoming barriers to become their best selves and were featured alongside influential women who have built organizations that are empowering women and making history.

- **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 fashion icon Victoria Beckham, rapper and songwriter Future, and American football pro bowler J. J. Watt. In 2018, music artist Cardi B, actress Gal Gadot, and UFC superstar Conor McGregor 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, Les Mills, and Midnight Runners. Most recently, Reebok announced the formation of the Boston Track Club, a professional running club with elite runners. Finally, continuing to build relationships with fitness instructors remains a crucial component of Reebok's goal of connecting with the global fitness community. With over 155,000 fitness instructors currently being part of its global network, Reebok has made major progress toward its goal to be the brand of choice for instructors around the world.
- **Digital ecosystem:** Reebok is changing the way it operates digitally in order 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. In 2018, Reebok improved site speed and usability of its consumer-facing digital ecosystem. Reebok is focused on continuing to optimize the consumer experience globally, with 2019 seeing a site redesign and the launch of a new membership program.

## ROLE OF THE CATEGORIES

To achieve the ambition of becoming the best fitness brand in the world, Reebok recognized the need to combine its performance authenticity with even better product and stronger lifestyle credentials for a consumer who is both fitness and style obsessed. To that end, Reebok combined its activities in Running and Training and created the Sport business. This unit, along with Classics, plays a vital role for the Game Changers, allowing the brand to amplify its impact on the fitness enthusiast and leverage commercial opportunities from their active lifestyle.

Sport's insight-driven and consumer-led approach supports authentic experiences for both highly specialized and versatile products. These products are at the forefront of fitness and true to the culture and community that the Game Changers train, run, and live in. Additionally, the Reebok Sport category has developed several contemporary silhouettes, which epitomize the intersection of performance, innovation and style. Reebok Classics celebrates the brand's unique heritage across multiple iconic silhouettes.

## 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. At the same time, 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, and the brand's margins have not been accretive to the company's overall profitability. As a result, Reebok announced a turnaround plan called 'Muscle Up' in 2016 aimed at accelerating Reebok's top-line growth in North America and improving the brand's overall profitability.

With efficient and effective distribution being key to Reebok's future success in the all-important North American market, the company has significantly reduced its store base in the market over the past two years. In total, the company has closed nearly 50% of its own stores in the US market – both concept stores and factory outlets – since the introduction of Muscle Up. In addition, the brand has also streamlined its wholesale business, putting a clear focus on elevating brand equity and driving profitable growth.

In addition to progressing on the brand's turnaround efforts in its home market, Reebok continues to execute on several transformational Muscle Up projects to enhance the profitability of the brand. Initiatives span marketing effectiveness, organizational efficiency and measures to improve product margins. By relentlessly executing against those initiatives Reebok has already realized meaningful profitability improvements, as reflected by the brand's increase in gross margin of 7.0 percentage points to 43.7% over the past two years.

While Reebok will continue to relentlessly execute the initiatives aimed at further improving its profitability, the brand will accelerate its efforts to drive high-quality revenue growth by shortening go-to-market timelines, driving product innovation, further focusing on its own e-commerce channel, and expanding partnerships with the most important wholesale customers.

## 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 actively shaping and accelerating the growth of our profitable and integrated trade network. 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, we continued to execute our 2020 strategic business plan, 'Creating the New', across our six global markets during 2018. At the beginning of the year, we completed the integration of the markets Greater China, Japan, South Korea and South-East Asia/Pacific into one consolidated market for Asia-Pacific. This allows us to better serve the converging consumer and customer demands in the region for 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 2,300 own-retail stores, more than 14,000 mono-branded franchise stores and more than 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. 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 online and brick & mortar). This is how we create halo effects across all consumer touchpoints, resulting in further marketplace expansion.

In 2018, we advanced our sales strategy with several initiatives focused, amongst others, on premium consumer experiences, marketplace transformation as well as productivity and efficiency 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' allows online shoppers to view in-store product availability.
- 'Click & Collect' allows consumers to order online and purchase or reserve items for pick-up in a local store.
- 'Ship from Store' allows us to service consumers faster than before by turning our stores into mini distribution centers.

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

#### Digital focus

In 2018, we continued our focus on and investments into digital partners. As part of our Partner Program initiative that was launched in 2016, we continued to successfully onboard partners across Europe, North America, Emerging Markets and Asia-Pacific, allowing us to deliver incremental sales growth and learnings that will be leveraged to evolve and further grow the program in the future. In addition, 2018 saw the expansion of the adidas App to a further 23 countries across all major markets, thereby becoming an important new consumer touchpoint in the adidas e-commerce ecosystem. 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 and access to our newly created membership program – the Creators Club. The success of the App is significantly enhanced by continued investments in Customer Relationship Management (CRM), which will enable us to develop an even 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*.  [SEE GLOSSARY](#) 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 online and brick & mortar). 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. In 2018, we made significant investments in remodeling our stores and sharpening the top of the pyramid of our store fleet. By doing so, we have strengthened our own retail presence in key cities and key trade zones. We extended our flagship fleet by opening a flagship store on Shanghai's East Nanjing Road and remodeled the existing Beijing Sanlitun store. 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. In that regard, we will continue to support our key wholesale partners, ensuring that we have premium space in their new flagship stores.

### Cities and trade zones

In the last couple of years, we saw continued success in our key cities New York, Los Angeles, Paris, London, Shanghai and Tokyo. Our *Net Promoter Score (NPS)* [SEE GLOSSARY](#) further improved year on year in our key cities during 2018,

helping to drive revenue growth to achieve our target to double revenues in our key cities by 2020 compared to the 2015 level. We will continue to focus on trade zones within the cities, specifically on how we deploy product, retail and activation initiatives. Our intention is to create one holistic brand experience for our consumers within these key commercial areas across all shopping channels and platforms.

### 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:** Our Sales Academy program continues to help 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 adidas 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 2018 we continued with our optimization program to shift focus and resources to our most profitable channels. By doing so, we have improved the distribution mix of our company and consequently the underlying profitability 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), market share, net sales, and profitability.

[SEE INTERNAL MANAGEMENT SYSTEM, P. 103](#)

# GLOBAL OPERATIONS

Global Operations manages the development, production planning, sourcing, and distribution of our company's products. The function strives to increase efficiency throughout the company's supply chain and ensures the highest standards in product quality, availability, and delivery. With the consumer in mind, we deliver competitively priced products in a sustainable manner, when and where they are wanted.

## CLEARLY DEFINED PRIORITIES FOR GLOBAL OPERATIONS

Global Operations delivers upon our company's mission to be the best sports company in the world. First, the function creates the best products by establishing state-of-the-art infrastructure, processes, and systems that enable us to focus on innovative materials and manufacturing capabilities. Second, Global Operations is focused on delivering best services through innovative distribution capabilities by enabling product availability through the omni-channel approach to supply chain agility. Third, Global Operations strives to deliver the best experience to our customers and consumers in a sustainable way.

**Best product:** 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 newness and increased speed-to-market capabilities. The function also plays a critical role in driving operational efficiency to support the company's growth ambition. Global Operations has been successfully consolidating and improving legacy structures, thereby reducing complexity and mitigating

material and labor costs for the company through material and packaging consolidation.

**Best service:** Global Operations strives to develop, produce, source, and distribute all ordered articles on time and in full. Therefore, a non-financial KPI 'On-Time In-Full' (OTIF) measures adidas delivery performance towards our customers and our own-retail stores.

**OTIF 2018** **78%** [SEE INTERNAL MANAGEMENT SYSTEM, P. 103](#) In 2018, adidas delivered 78% of its adidas and Reebok brand products on time and in full (2017: 78%), which is broadly in line with the overall target of 80%. In Greater China and Russia/CIS, OTIF levels reached above 90% of our order quantities.

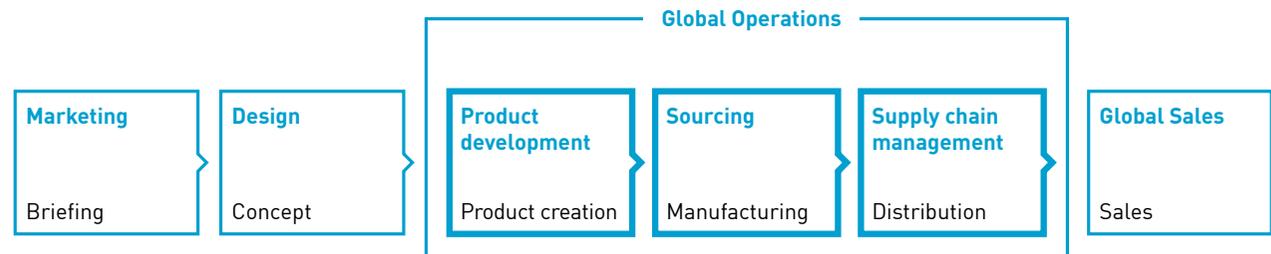
**Best experience:** Global Operations contributes to the adidas strategic business plan 'Creating the New' to accomplish our mission. The function strengthens brand desire by creating and providing the right product to consumers – in the right quality, size, color, and style, in the right place and at the right time, across the entire range of the company's channels and brands. Global Operations builds capabilities that further improve supply chain efficiencies, while mitigating costs, thereby ensuring a continuously sustainable and competitive

supply chain. Global Operations is driving several strategic initiatives to push Creating the New.

## STRATEGIC COMPANY PRIORITY 'SPEED'

'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](#) We are consumer obsessed; thus, we want to respond quicker to consumer demand. We want to make our products available when and where they are wanted across our wholesale, retail, and e-commerce channels. Our aim is to always be on trend and always in stock. We are moving away from predominantly developing products in advance of seasonal merchandising calendars and are getting closer to responding quickly to consumer demands with in-season development and rapid replenishment manufacturing. 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. In 2018, we made further progress around our strategic priority with advanced creation and production capabilities and we are working to achieve at least 50% of the company's net sales through speed-enabled articles by 2020. With the 'Speed' initiative, we expect to increase sales and achieve

Global Operations in go-to-market process



a higher share of full-price sell-through compared to the regular range.

**Advanced production capabilities:** To increase ‘Speed’ also on production timelines, in 2018 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 for the vast majority of our footwear, apparel and hardware products. In addition to shortening our overall production lead times, Global Operations has scaled its fast replenishment capabilities of best-selling articles, offering more articles within seasons based on actual sell-through data, with 20% of all articles across all product categories established on 30 days production lead times.

**Speedfactory:** Powered by end-to-end automated manufacturing processes and innovative materials, with *Speedfactory* [SEE GLOSSARY](#) we create high-quality performance products faster than ever before to react to moments that matter in key markets. With that we also enable our key customers to co-create in an interactive production process while creating customer engagement and ultimately brand desire. Insights gained from our Speedfactories will enable us to drive digital manufacturing also into our existing supply chain. [SEE CORPORATE STRATEGY, P. 62](#)

### DIGITALIZING THE END-TO-END CREATION-TO-SHELF VALUE CHAIN

In recent years Global Operations has focused on digitalizing the product creation process, leveraging digital capabilities and technologies across design and development teams. In 2018, we further expanded these efforts towards digitalizing the end-to-end creation-to-shelf value chain. This covers the pre-season marketing planning phase to product design, development, sourcing, and into the sell-in process. This is

now established as a key strategic priority under the umbrella of digital transformation.

To connect the end-to-end value chain, we have brought key building blocks together and we aim to scale up our new way of working with one of our Business Units. With digitally created products we support a more efficient creation process internally enabling a ‘right first-time’ approach. Externally, digital products will become more prominent in the interaction and communication with our partners, allowing us to make faster product iterations and take better decisions earlier in the process. This new way of working will enable a faster time-to-market and create a holistic and immersive digital sell-in experience for our key customers. Our ambition in 2019 is to continue building the digital infrastructure for the future, gradually rolling out the new capabilities across our businesses, and extending the platform to invite consumers to co-create with us, while also working closer with our key customers in the early phases of the creation process.

### FUTURE OF MATERIAL SOURCING

Global Operations constantly looks 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](#), in 2018, we continued 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 and other sustainable materials, we built a dedicated sourcing operation with the aim to ensure a steady and transparent supply chain. We expanded our sourcing countries for ocean plastic in 2018 from Maldives to Sri Lanka and will continue to grow in 2019, focusing on South East Asia and expanding collaboration with Small Island Development States. We developed a code of conduct specific to the plastic collection

and processing that is now applied by our selected partners operating in countries in scope. [SEE SUSTAINABILITY, P. 88](#)

### AUTOMATION TO IMPROVE PRODUCTION EFFICIENCY

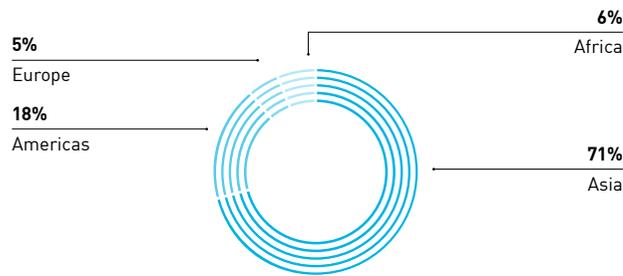
Driving the level of automation in our supply chain remains of overriding importance for Global Operations. In this context, automation technologies such as auto cutting, computerized stitching, robotic adhesive spray system, and auto packing solutions are important focus areas, as they allow us to reduce our dependency on manual labor while ensuring consistent and highest quality standards. To further improve our production efficiency, we will continue to increase the level of automation in our supply chain in the years to come.

### MAJORITY OF PRODUCTION THROUGH INDEPENDENT MANUFACTURING PARTNERS

[F](#) To keep our production costs competitive, we outsource almost 100% of production to independent manufacturing partners (adidas only operates two own production sites – one in the USA and one in Germany). In 2018, adidas changed the definition of independent manufacturing partners from individual manufacturing facilities to supplier group level (i.e. companies we work with that might produce in several manufacturing facilities). Based on this new definition, we worked with 130 independent manufacturing partners in 2018 that were producing in 289 manufacturing facilities (2017: 296).

Of our independent manufacturing partners, 71% are located in Asia (2017: 79%), 18% in the Americas (2017: 11%), 6% in Africa (2017: 1%), and 5% in Europe (2017: 9%). [SEE DIAGRAM 23](#) While we provide our manufacturing partners with detailed specifications for production and delivery, they possess excellent expertise in cost-efficient, high-volume production of footwear, apparel, and *hardware*. [SEE GLOSSARY](#)

**Independent manufacturing partners by region<sup>1</sup>** 23



<sup>1</sup> Figures include the adidas and Reebok brands, but exclude local sourcing partners, sourcing agents, subcontractors, second-tier suppliers and licensee factories.

In line with the definition change from individual manufacturing facilities to supplier group level, 26 of the 130 independent manufacturing partners are considered key strategic partners and produce the vast majority of our products in

**Key strategic partner relationships** 24

	Total	Footwear	Apparel	Hardware
Number of key strategic partners	26	11	8	7
Average years as key strategic partner	17.8	17.0	17.2	19.6
Share of all production volume	74%	92%	62%	54%
Share of all production value	78%	92%	57%	61%
Strategic relationships < 10 years	15%	18%	13%	14%
Strategic relationships 10 – 20 years	42%	36%	63%	29%
Strategic relationships > 20 years	42%	45%	25%	57%

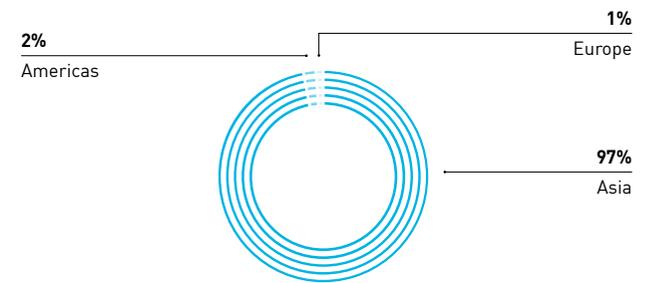
82 manufacturing facilities worldwide (2017: 109). We value long-term relationships: 84% of our key strategic partners have worked with adidas for more than ten years and 42% have a tenure of more than 20 years. [SEE TABLE 24](#)

The length of the relationship is determined by specific performance criteria which are regularly measured and reviewed by Global Operations. To ensure the high quality that consumers expect from our products, we enforce strict control and inspection procedures of our manufacturing partners 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](#) Current supplier lists can be found on our website. [ADIDAS-GROUP.COM/SUSTAINABILITY/S/SUPPLY-CHAIN-APPROACH](#)

**VIETNAM REMAINS LARGEST FOOTWEAR SOURCING COUNTRY**

97% of our total 2018 footwear volume was produced in Asia (2017: 97%). Production in Europe and the Americas combined accounted for 3% of the sourcing volume (2017: 3%). [SEE DIAGRAM 25](#) Vietnam represents our largest sourcing country with 42% of the total volume (2017: 44%), followed by Indonesia with 28% (2017: 25%) and China with 18% (2017: 19%). In 2018, our footwear manufacturing partners produced approximately 409 million pairs of shoes (2017: 403 million pairs). [SEE DIAGRAM 26](#) Our largest footwear factory located in Vietnam produced approximately 11% of the footwear sourcing volume (2017: 11%).

**Footwear production by region<sup>1</sup>** 25



<sup>1</sup> Figures include the adidas and Reebok brands.

**Footwear production<sup>1</sup> in million pairs** 26



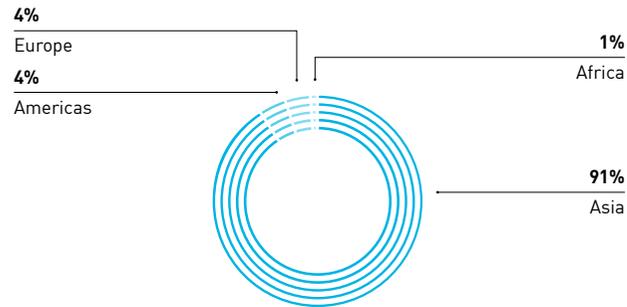
<sup>1</sup> Figures include the adidas and Reebok brands.

**CAMBODIA BECOMES LARGEST SOURCE COUNTRY FOR APPAREL**

In 2018, we sourced 91% of the total apparel volume from Asia (2017: 93%). The Americas represented 4% of the volume, Europe 4%, and Africa 1% (2017: the Americas 4%, Europe 3%, and Africa 1%). [SEE DIAGRAM 27](#) Cambodia is the largest sourcing country, representing 24% of the produced volume (2017: 22%), followed by China with 19% (2017: 23%) and Vietnam with 18% (2017: 18%). In total, our manufacturing partners produced approximately 457 million units of apparel

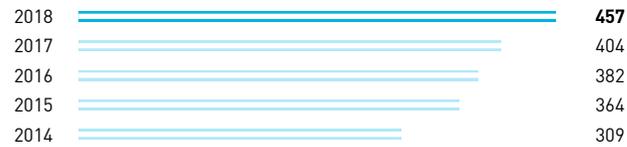
in 2018 (2017: 404 million units). [SEE DIAGRAM 28](#) The largest apparel factory produced approximately 9% of this apparel volume and is located in China (2017: 10%).

**Apparel production by region<sup>1</sup>** 27



<sup>1</sup> Figures include the adidas and Reebok brands.

**Apparel production<sup>1</sup> in million units** 28

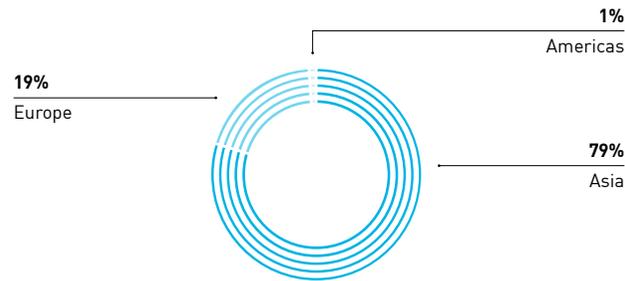


<sup>1</sup> Figures include the adidas and Reebok brands.

**CHINA REMAINS MAIN SOURCE OF HARDWARE PRODUCTS**

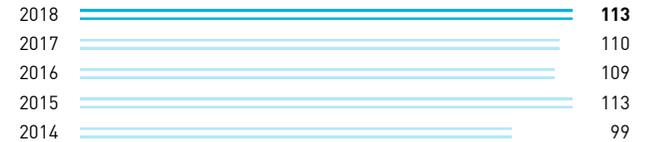
In 2018, 79% of our hardware products, such as balls and bags, were produced in Asia (2017: 82%). Europe accounted for 19% (2017: 16%) and the Americas represented 1% of the total volume (2017: 2%). [SEE DIAGRAM 29](#) China remained our largest sourcing country, accounting for 38% of the sourced volume (2017: 40%), followed by Turkey and Pakistan with 18% each (2017: 15% and 18%, respectively). The total hardware sourcing volume was approximately 113 million units (2017: 110 million units), with the largest factory accounting for 18% of production (2017: 15%) located in Turkey. [SEE DIAGRAM 30](#)

**Hardware production by region<sup>1</sup>** 29



<sup>1</sup> Figures include the adidas and Reebok brands.

**Hardware production<sup>1</sup> in million units** 30



<sup>1</sup> Figures include the adidas and Reebok brands.

**INCREASED AVAILABILITY BY OPTIMIZING THE DISTRIBUTION CENTER NETWORK**

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 for pick-up in our own-retail stores or own-retail stores able to sell inventory available in other own-retail stores. [SEE SALES AND DISTRIBUTION STRATEGY, P. 72](#)

In 2018, Global Operations focused on further optimizing its distribution center network, while at the same time preparing it for future consumer demand. In this context, we extended one distribution center on a large scale in Rieste, Germany and built a new distribution center in Suzhou, China – both went live in 2018. In addition, we started with the construction of a new distribution center in Pennsylvania, USA and expanded our existing West Coast third-party 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 as well as to position us well for Brexit, we added a new e-commerce facility to our existing distribution network in the market in 2018.

# INNOVATION

**Creating innovative concepts to meet the needs of athletes and 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 concept pipeline, bringing new groundbreaking technologies and processes to life, investing into sustainable enablers and exploring the 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.**

## 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.

During 2018, adidas continued to implement a centralized project team to drive the process for the application and

management of publicly funded research projects. Located within the FUTURE team, the team is responsible for collaborating with governmental organizations on a local, national and European level to develop key projects with strong consortia partners, tackling major societal challenges that will impact our consumer and industry. Three major projects were finalized in 2018, spanning research on a new class of fully recyclable sporting goods, on human/computer interaction concepts for wearable computing trends, and on the development of an entire eco-system for innovative internet-based services catering to the consumer.

## INNOVATION APPROACH BASED ON OPEN SOURCE MINDSET

Our approach to innovation 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 the input from knowledgeable partners. We work with several partners to unlock further potential through collaborations:

- **BASF:** Together with BASF we manage and enhance BOOST, an industry-first cushioning technology designed to deliver maximum energy return, responsiveness and comfort to athletes.
- **Carbon:** Together with Carbon, a Silicon Valley-based tech company, we are revolutionizing product creation through hardware, software and molecular science, to enable mass production of additively manufactured components, coming to life with adidas 4D.
- **Fashion for Good:** Together with Fashion for Good, a global initiative to make all fashion sustainable, we are accelerating and scaling sustainable innovation in the apparel industry through, among other things, mentorship of circular apparel start-ups.

- **Oechsler:** Together with Oechsler, an expert in high-tech automated manufacturing of technical components and assemblies, we operate our Speedfactories in Ansbach, Germany, and Atlanta, USA.
- **Parley for the Oceans:** Together with Parley for the Oceans, we are developing products partially created from upcycled plastic waste, intercepted before it reaches the ocean from beaches and coastal communities.

## 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, 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 consumer, it is crucial to fully understand the specific product needs of the female athlete 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.

## COMMERCIALIZATION OF INNOVATIONS

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

- **adidas 4D:** The high-performance footwear produced under the adidas 4D concept features midsoles crafted with light and oxygen using Digital Light Synthesis, a unique technology developed by Carbon. The 4D midsole pioneers a digital footwear component creation process that eliminates the necessity of traditional prototyping or molding. With the new technology, adidas officially departs from 3D printing and brings additive manufacturing in the sports industry into a new dimension. adidas produced more than 100,000 pairs of this high-performance footwear in 2018 and is working with Carbon to develop new machinery to continue scaling for mass production. Futurecraft 4D, the first shoe to feature a 4D midsole, was recognized with the 'Gold Lion Design' and the 'Silver Lion Innovation' awards in Cannes in 2018.
- **Parley Ocean Plastic:** Products made of *Parley Ocean Plastic* [SEE GLOSSARY](#) focus both on the needs of our athletes, by living up to their performance promise, and on the needs of the world, by helping to protect our oceans from marine plastic pollution. We have taken sustainability to the product level and continue to roll it out across our product portfolio. In 2018, we made five million pairs of shoes containing Parley Ocean Plastic, across various footwear franchises in both Sport Performance and Sport Inspired. In addition, two million pieces of our 2018 apparel offering featured Parley Ocean Plastic, including jerseys for high-profile teams such as Real Madrid, Bayern Munich, Juventus Turin and Manchester United.
- **AM4 Series:** The 'adidas made for (AM4)' products are created at the adidas Speedfactory facilities in Ansbach and Atlanta. In 2018, we launched AM4 products for Los Angeles (AM4LA), New York (AM4NYC), Shanghai (AM4SH)

and Tokyo (AM4TKY), completing the 'Key City Series' which started with London (AM4LDN) and Paris (AM4PAR) in 2017. During 2018, there were additional AM4 limited editions specific to cultural and sporting moments, such as the AM4NHL which was built in the Atlanta Speedfactory to reward the 2018 Stanley Cup winner Washington Capitals. Each run is bespoke product tailored to unique demands and local insight, produced at speed and scale.

- **Creators Club:** This new digitally enabled membership program rewards loyal consumers with invitations to exclusive events and access to limited-edition products. In addition, it enhances the e-commerce shopping experience for members through an even faster checkout process and new order-tracking options. The program allows us to deepen the relationship with our consumers and to gain valuable insights into their expectations and needs. Creators Club launched in the US toward the end of 2018, with other markets to follow in 2019.
- **PureMove Bra:** Treated with Motion Sense Technology, the Reebok PureMove Bra changes the game for women's sports bras. The PureMove Bra will naturally stiffen when high-intensity workouts begin, and releases when complete for comfort. Based on strong consumer feedback on the launch, this exclusive material is now being modeled into more extended sizes and additional applications. For the PureMove Bra initiative, Reebok partnered with the University of Delaware.
- **Cotton + Corn:** Reebok's Cotton + Corn is the first bio-based shoe, certified in the US and Western Europe, and 'made with things that grow': an upper comprised of organic cotton and a base originating from industrial grown corn, which is a non-food source. Cotton + Corn was also launched in a vegan version and will be extended to multiple colorways in upcoming seasons. For the Cotton + Corn initiative, Reebok partnered with DuPont Tate & Lyle Bio Products, a leading manufacturer of high-performance bio-based solutions.

## 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 2018. 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 over-proportionately to net income in 2018. We expect this development to continue in 2019 as we will present a wide range of new, innovative products. [SEE OUTLOOK, P. 128](#)

In 2018, 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 74% of brand sales (2017: 79%), while only 3% of sales were generated with products introduced three or more years ago (2017: 2%). At Reebok, 67% of footwear sales were generated by products launched in 2018 (2017: 69%). Only 11% of footwear product sales relate to products introduced three or more years ago (2017: 12%).

## R&D EXPENSES DECREASE 18%

Expenses for research and development (R&D) include expenses for personnel and administration, but exclude other costs, for example costs associated with the design aspect of the product creation process or the majority of costs related to company-wide Open Source initiatives. In 2018, as in prior years, all R&D costs were expensed as incurred. The company's R&D expenses decreased 18% to € 153 million from € 187 million in the prior year.

In 2018, R&D expenses as a percentage of sales equated to 0.7% (2017: 0.9%). The number of people employed in R&D activities at December 31, 2018, was 1,041 compared to 1,062 employees in the prior year. This represents 1.8% of total employees. [SEE TABLE 31](#)

### Key R&D metrics<sup>1,2</sup>

31

	2018	2017	2016	2015	2014
R&D expenses (€ in millions)	153	187	149	139	126
R&D expenses (in % of net sales)	0.7	0.9	0.8	0.8	0.9
R&D employees	1,041	1,062	1,021	993	985

<sup>1</sup> 2018, 2017 and 2016 figures reflect continuing operations as a result of the divestiture of the Rockport, TaylorMade, Adams Golf, Ashworth and CCM Hockey businesses.

<sup>2</sup> 2015 and 2014 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 32](#) 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 2018, we made good progress by advancing the following initiatives.

### ATTRACTION AND RETENTION OF THE RIGHT TALENTS

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 2018, adidas locations around the world leveraged

our employer brand attributes for attraction, retention and engagement strategies. This work contributed to several top rankings worldwide, including the Glassdoor and LinkedIn Best Employer rankings, as well as Best Employer in Digital Talent Communication. This has also helped us to attract some of the industry's top talent.

Our offices in China, Hong Kong, Italy, the Netherlands, South Africa, Spain, Taiwan, and the United Arab Emirates received the Top Employer Institute awards in 2018 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 and 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.

### ROLE MODEL LEADERSHIP

The quality of current and future talent and leadership is key to our success. We want to inspire and nurture role model leadership. 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 have tailored individual development plans and participate in targeted development programs. These are complemented by dedicated apprenticeship and trainee programs to attract great talent.

In 2018, we made further progress with this People Strategy pillar.

The four pillars of our People Strategy



### Leadership groups

We have established three groups with selected leaders and talents within the company:

- The **Core Leadership Group** (CLG) is the most senior group, made up of around 20 members from our senior leadership population. Members of this group jointly represent critical positions and roles across our company worldwide. This group partners with the Executive Board in leading the execution of the Creating the New strategy, accelerating its delivery across functions, as well as developing and inspiring the next generation of leaders. The CLG also serves as the succession pool for the Executive Board.
- The **Extended Leadership Group** (ELG) has around 120 members. The ELG collaborates across markets and functions to lead the execution of the strategic initiatives that form the Creating the New portfolio, and drives continuous improvement and consistency across the organization. The ELG also mentors and sponsors the Global High Potential Group and serves as a succession pool for the CLG.
- The **Global High Potential Group** (GHIPO) was formed in 2018 consisting of around 50 members with an equal gender balance. The GHIPO group enables us to identify and develop high potentials who have the ability to take on more complex, demanding and higher-level responsibilities at a global senior management level.

We hold two physical-presence CLG and ELG events per year, together with the Executive Board, to ensure these groups interact and align on the execution of Creating the New as well as our People Strategy. The GHIPO also meets twice per year for an on-site learning experience in our key markets. Throughout the year, all groups remain in touch via virtual meetings and calls. [SEE CORPORATE STRATEGY, P. 62](#)

### Leadership Framework

To drive clarity and accountability, leaders at adidas were engaged to further activate our global *Leadership Framework* [SEE GLOSSARY](#) in 2018. The Leadership Framework is based on the three company behaviors creativity, collaboration and confidence (the '3Cs' [SEE GLOSSARY](#)) 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 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 is built into the way we hire and promote as well as rate performance. The framework was first activated and cascaded to employees globally through the CLG and ELG groups.

### Leadership development experiences

We offer a portfolio of leadership development programs for corporate office employees for all grades and levels:

- **Executive Development Experience:** We are partnering with Harvard Business School in delivering a tailored learning experience for all of our senior manager population. In 2018, the CLG and ELG attended the in-residence Executive Development Experience at Harvard Business School. The rest of our senior managers are experiencing the same content in a live-virtual online learning setting.
- **Manager Development Experience and Director Development Experience:** In an effort to develop current and future leaders of our company, we introduced the Manager Development Experience (MDE) in 2018. MDE is a flexible approach to develop the leadership skills and abilities of our lower management level employees. MDE is designed to provide a customizable learning experience that uses the Leadership Framework as its foundation and drives the development of personal and team mastery. MDE is inspired by sport – what can the world of sport teach

leaders about managing themselves and others? In 2019, we will introduce the Director Development Experience (DDE). DDE is based on the same principles with the Leadership Framework at its core and allows a customizable learning experience for our middle management level employees.

- **Talent Carousel:** Our internal career development program Talent Carousel has entered its fourth year, with the second generation graduating in 2018. 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.

### Succession management

Our succession management approach aims to ensure stability and certainty in business continuity through the development of strong internal pipelines for our critical leadership positions. We achieve this through a globally consistent succession process that identifies these important leadership positions within the organization, and matches identified top talent as successors for these roles. We conduct regular reviews to ensure individual development plans are in place to prepare successors for their potential next steps. The leadership groups we have established serve as succession pools for the highest levels of our organization.

### Future talent programs

- **Apprenticeship and Dual Study Program:** The adidas Apprenticeship Program offers young pupils 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, IT or other areas. The Dual Study Program for young school graduates offers – in cooperation with

various universities – theoretical and practical experience at adidas in fields such as digital commerce, finance or international business including at least one three- to six-month international rotation. At the end of 2018, we employed 55 apprentices in Germany (2017: 65) and 45 Dual Study Program students (2017: 37).

- **Global Trainee Program:** The Functional, Digital and Design Trainee Program is an 18- to 24-month program providing graduates with an international background and excellent educational credentials the opportunity to start a functional career within adidas. The program comprises assignments in various functional and cross-functional departments. At least one of these assignments takes place abroad. At year-end 2018, we employed 61 participants in our Global Trainee Program (2017: 63).
- **Internships:** Our global internship program offers students three to six months of work experience within adidas. In 2018, we employed 447 interns in Germany (2017: 765).

### 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 for 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 managers and the Executive Board.

Via a-LIVE we offer all employees access to the Learning Campus, where employees are able to utilize learning opportunities 24/7 in a virtual environment. We also offer in-person learning activities. As a result of the global implementation of our Learning Management System that continued through 2018, we have increased the accessibility

of employee training and development activities across the globe. Through the Learning Campus, our people are able to develop skills to support their current performance and future career development. In 2018, 21,228 employees (2017: 23,113) accessed our Learning Campus digitally, while 6,810 employees (2017: 4,295) employees participated in in-person learning activities, ranging from two hours to two days in duration. In mid-2018, we launched the LinkedIn Learning platform, giving all corporate office employees access to content across subjects in business, creative and technology areas. Employees who accessed this digital learning content in the first six months spent an average of around 70 minutes per month on self-directed learning. This uptake of learning is in the upper third of benchmarks for global organizations.

In 2018, adidas core learning programs were launched 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.

### DIVERSITY AND INCLUSION

We believe it is crucial for the success of our company to have a diverse workforce comprised of 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 fulfill 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.

Nationalities at  
HQ in Germany

> 100

At our company's headquarters in Herzogenaurach, Germany, 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. Throughout the company we continue to support our Employee Resource Groups – specific networks that give employees from various walks of life a voice. We have women's networks in North America, Latin America, Europe and Asia, LGBTQ networks in North America and Europe as well as a network to connect people with different ethnic backgrounds in North America, and an experienced generation network in Europe.

The Executive Board and senior management teams are provided with quarterly diversity reporting to support decision making and target setting, and we continue to invest in diversity and gender intelligence training across the organization.

In 2018, functional and local market teams continued to develop dedicated action plans to invest in a stronger female talent pipeline, data analysis on gender balance and a more balanced organization in terms of gender, age and origin. As an example, Latin America saw a notable increase in the female leadership ratio throughout the year as a result of intensified efforts in driving a set of initiatives. This included a significant increase in the number of employees receiving gender intelligence training, the initiation of senior leadership mentoring with a balanced 50:50 ratio, as well as the launch of 'Lean In' learning circles, a concept and reference tied to our partnership with the 'Lean In' organization.

To inspire action outside of our company, we are active members in both 'Charta der Vielfalt' ('Diversity Charter') and the Diversity and Inclusion in Asia Network (DIAN), that allow us to promote communication and the sharing of best practices and insights. adidas is also listed in the genderdex and has become a member company within the Bloomberg Gender-Equality Index.

### Gender intelligence training

We continued the delivery of our global 'BIG Deal' gender intelligence training, with 300 senior managers upskilled in 2018, resulting in a total of over 600 employees since the launch of the training in 2016. 'BIG' stands for Balanced, Inclusive, Gender Intelligent, and 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 re-visit and think critically about some of their key thoughts and beliefs around diversity, stereotyping and bias in the workplace. BIG Deal training will become part of the Director Development Experience. Moreover, we have made the move to internalize the delivery of the BIG Deal training with a Train the Trainer program to increase the roll-out speed and scope. Thus far, a total of almost 30 internal facilitators have been upskilled – with training delivered to around 900 colleagues in North America in 2018. Our headquarter-based facilitators in Germany will initiate delivery of BIG Deal training in 2019.

### 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 Global High Potential 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 globally. By the end of 2018, the company had recorded a

### Women in management positions

33%

Participation of Women and Men in Leadership Positions in the Private and Public Sector', the adidas AG Supervisory Board determined target figures for the percentage of female representation on the Executive Board, including corresponding deadlines for their achievement, and the Executive Board determined such target figures for the first two management levels below the Executive Board, including deadlines for their achievement, for adidas AG.

SEE CORPORATE GOVERNANCE REPORT INCLUDING THE DECLARATION ON CORPORATE GOVERNANCE, P. 35

### CULTURE

It is our goal to develop a culture that cherishes creativity, collaboration and confidence (the 3Cs) as well as high performance – the behaviors we deem crucial to the successful delivery of our corporate strategy. In fact, our culture and people serve as the foundation and a key enabler of the Creating the New strategy.

### Performance management

To drive high performance within the company, in 2018 we replaced our performance management approach called 'The Score' with '#MYBEST', which is a new and holistic performance development approach combining monthly high-quality conversations between the employee and the line manager as well as regular upward and peer feedback options with quarterly target setting and performance evaluation.

The approach is based on the evaluation of multiple dimensions:

- **Target achievement:** qualification of how well an employee has delivered upon established quarterly objectives

total of 33% of women globally in management positions (2017: 31%), exceeding the 2020 target of 32%.

ADIDAS-GROUP.COM/S/EMPLOYEES Pursuant to the German 'Law on Equal

- **Behaviors:** qualification of how well an employee is living the company Leadership Framework and 3C behaviors
- **Peer and upward feedback:** employees can request and incorporate feedback from colleagues and direct reports in their overall assessment for a more holistic review.

### Wages, benefits and incentives

We are committed to rewarding our employees with compensation, benefit and incentive programs that are competitive in the marketplace and are aligned with our performance culture. 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 senior management 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 the 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 compensation adjustment approach. The approach was introduced in Germany and the US in 2017 and 2018, and is designed 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 to ensure that we pay equally at the same level for female and male employees. Furthermore, we developed a monitoring approach to identify potential pay gaps and work continuously to improve and close these gaps on a country-by-country basis. To further enhance our efforts and transparency on this topic we support initiatives such as 'Lean In' and will also in 2019 put a strong emphasis on continuously closing potential gaps.

In addition, we improved transparency and governance for senior 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 rolled out a 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 a company ownership mentality. [SEE NOTE 28, P. 189](#)

Our subsidiaries also grant a variety of benefits to employees, depending upon locally defined practices and country-specific regulations and norms.

#### Stock Purchase Plan

Participation in the Stock Purchase Plan is provided to employees in Germany, the US, the Netherlands and Greater China (China mainland, Taiwan and Hong Kong), offering 45% of the total employee population the possibility to participate.

By the end of 2018, approximately 4,800 employees (2017: 3,600) participated in the program.

#### Work-life integration

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 the provision of flexible working times 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 two day-care facilities at our headquarters in Herzogenaurach, Germany. After opening our first full-time care center 'World of Kids I' that offers places for 130 children aged three months to school entry age in 2013, an outdoor group with 20 additional places for kindergarten children was added in 2017, as well as the second facility 'World of Kids II' in 2018, providing 138 spots for nursery and kindergarten children. In 2019, this will be complemented by 15 ad hoc places to support all parents in emergency situations or during short-term assignments. On-site, our external partners are upskilled and trained on an educational approach that is based on our company values such as creativity, diversity and inclusion, democracy, health and movement. Additionally, World of Kids is among 100 digital leading model childcare centers in Germany and has been supported with technical equipment (e.g. iPads or cameras for kids). Other global locations also offer various forms of benefits and support services to ensure that our employees are able to access and secure quality childcare. With the ongoing expansion of our infrastructure and childcare offering, we as a company emphasize our commitment to a family-friendly environment to integrate work and private life – and enable balanced careers.

For parental leave and re-entry, programs are in place to provide employees with advice early on and options for their return to work, also taking into consideration flexible working hours and work locations. In Germany, we guarantee our employees on parental leave their positions, which are only filled temporarily. In the US, in addition to regular parental leave for new parents (up to 10 weeks at home, 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.

Continuing in Germany in 2018, every employee with an adidas AG contract whose working tasks can be carried out independently of campus facilities, campus equipment or personal interaction on-site is eligible to work 20% of their total working time off-campus. This new policy and agreement is based on our belief that results can be achieved in the same quality and quantity, regardless of people's location. Over the course of the year we evaluated our off-campus working approach in Germany. Approximately 3,400 employees took part in a survey, and based on the positive feedback we decided to roll out the off-campus working approach globally. Our North America market implemented the concept in November, and additional markets will begin the implementation process in 2019.

In line with the expansion efforts at the headquarters campus in Herzogenaurach, in 2018 we opened HalfTime, a 14,000m<sup>2</sup> event center with integrated employee restaurant that is designed with an open floor plan and with rooms that are adaptable to different configurations, such as private meetings, discussions and workshops. In 2019, a new building

called Arena will become the company’s new main office with capacity for around 2,000 employees, centralizing most of the employees in Herzogenaurach on the World of Sports campus. Continuing the successes of our newly established workplace spaces (called BASE, Pitch 1 and Pitch 2), we are integrating the activity-based working concept, which means that employees no longer have assigned desks and instead choose from a variety of rooms and spaces, dependent on their needs.

**MEASURING THE SUCCESS OF OUR PEOPLE STRATEGY**

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 the goal 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 desirable 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, in 2017 we launched ‘People Pulse’ – our approach and system platform for measuring the level of employee satisfaction with the experience adidas provides as an employer – for all office employees with an email account.

People Pulse allows for the measurement of employeeNPS (eNPS). [SEE INTERNAL MANAGEMENT SYSTEM, P. 103](#) 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 approach as well as a 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 in every survey to allow for tracking of the results over time.
- Changing focus topics which are directly derived from the company’s strategic agenda as well as the new Leadership Framework and the 3Cs.

In 2018, we saw People Pulse gain significant traction, to a point where it is now fully embedded within the organization globally. 90% of eligible employees participated at least once over the course of the year. We place a major focus on delivering an effective insights-to-action process, which was achieved through a change of cadence from monthly to quarterly tracking as of July 2018 for additional depth of insights, centralized tracking of action plans and the creation of a global People Pulse Ambassador community to facilitate sharing of successes and best practices.

Company-wide focus on eNPS and influencing factors, as well as on targeted follow-up actions and communication, led to a positive trend in eNPS in 2018. We now not only leverage People Pulse for general feedback on the employee experience

at adidas, but also as a tool to gather employee insights regarding important elements of our strategy such as Brand Leadership or Leadership Framework adoption.

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 2018
Reporting of People Pulse results	<ul style="list-style-type: none"> <li>– Reports with scores and anonymized comments are provided to the Executive Board as well as leaders down to the Board -3 level.</li> <li>– Employees have access to the overall company results via a SharePoint workspace and our global intranet a-LIVE.</li> </ul>
Minimum participation rate per quarter of 50% and accumulated participation rate of 80% at least once every six months	<ul style="list-style-type: none"> <li>– Participation in 2018 rose to 60% on average per pulse.</li> <li>– More than 90% of eligible employees participated in at least one pulse.</li> </ul>
Results recipients to, among others, <ul style="list-style-type: none"> <li>– actively show leadership commitment and ownership by openly discussing the results</li> <li>– drive action on identified areas of improvement</li> </ul>	<ul style="list-style-type: none"> <li>– Leaders partner with HR and relevant functions to review, cascade and communicate results.</li> <li>– Discussion with network of ‘People Pulse Champions’ to share best-practice examples.</li> </ul>

**HR FOUNDATIONS FOR OUR PEOPLE STRATEGY**

In 2018, the adidas HR function defined and kicked off a multi-year HR Cloud transition roadmap to strengthen, future-proof and further enhance the HR system landscape of the company. The cloud transition will further drive standardization, digitization and automation across HR to scale, as well as enable HR to proactively manage the workforce and enable the organization to increasingly make data-driven decisions.

In 2018, we also focused on further enhancing and expanding the HR Shared Service Center function for Germany to also cover services for the Netherlands. In addition, a second HR Shared Service Center has been launched and established out of Portland to provide services for North America. 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 second half of 2018, the HR Shared Service Center functions were organizationally consolidated into a cross-functional Global Business Services (GBS) business unit to further professionalize the company's shared services approach.

## GLOBAL EMPLOYEE POPULATION

On December 31, 2018, the company had 57,016 employees (2017: 56,888). Thereof, **57,016** 7,830 were employed at adidas AG. [SEE TABLE 33](#) On a full-time equivalent basis, our company had 49,563 employees (thereof 7,182 adidas AG) on December 31, 2018 (2017: 48,775). [SEE TABLE 34](#) Personnel expenses decreased to € 2.481 billion in 2018 (2017: € 2.549 billion), representing 11% of sales (2017: 12%). [SEE NOTE 35, P. 212](#) An overview of the development of our employee base in the past ten years can be found in the ten-year overview. [SEE TEN-YEAR OVERVIEW, P. 240](#)

### Employee statistics<sup>1</sup> 33

	2018	2017
Total number of employees <sup>2</sup>	57,016	56,888
Total employees		
Male	51%	50%
Female	49%	50%
Management positions		
Male	67%	69%
Female	33%	31%
Average age of employees (in years)	31	30
Average length of service (in years)	4	4

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

<sup>2</sup> Number of employees on a headcount basis.

### Number of employees by function<sup>1</sup> 34

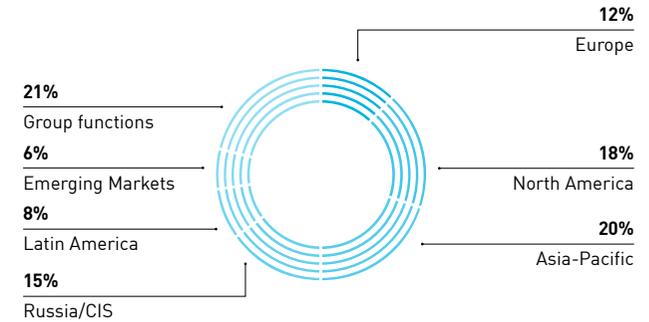
	Employees <sup>2</sup>		Full-time equivalents <sup>3</sup>	
	2018	2017	2018	2017
Own retail	32,297	32,698	25,880	25,640
Sales	3,857	3,795	3,742	3,680
Logistics	6,175	5,890	5,976	5,617
Marketing	5,764	5,964	5,565	5,742
Central administration	5,574	5,157	5,251	4,835
Production	888	1,132	803	1,105
Research and development	1,041	1,062	971	1,002
IT	1,420	1,190	1,377	1,154
<b>Total</b>	<b>57,016</b>	<b>56,888</b>	<b>49,563</b>	<b>48,775</b>

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

<sup>2</sup> Number of employees on a headcount basis.

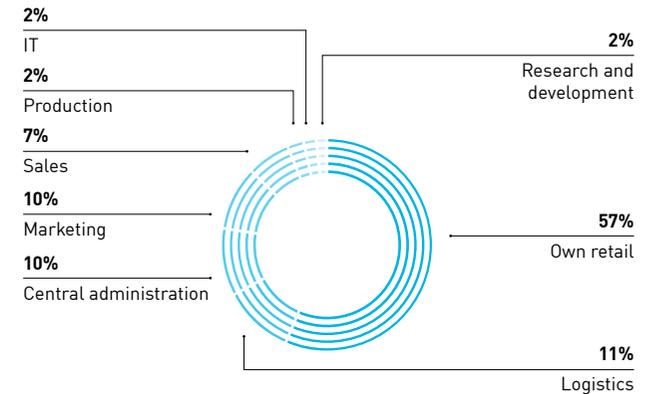
<sup>3</sup> Number of employees on a full-time equivalent basis; deviations in totals may arise due to calculation of full-time equivalents.

### Employee split<sup>1</sup> 35



<sup>1</sup> At year end.

### Employees by function<sup>1</sup> 36



<sup>1</sup> 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 company 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. We have a clear roadmap for 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 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 formal 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. Our ongoing evaluation of these topics in 2018 has shown that we can confirm our strategic ambitions and embedded goals that we aim to reach by 2020.

[SEE NON-FINANCIAL STATEMENT, P. 101](#)

We are using external frameworks to determine the selection of material topics, and to ensure alignment with global development priorities. One of these frameworks is the UN Sustainable Development Goals (SDGs) which represent a global call for action to promote prosperity for all while protecting the planet. We have used internal and external methods that helped us identify the SDGs on which we believe our business has the most impact, and where our sustainability roadmap can lead to positive impact. Although our current roadmap and underlying targets were implemented prior to the adoption of the SDGs, we see a clear correlation between the SDGs and our own commitment to sustainable development. Consequently, we have been able to link prioritized SDGs with both the environmental priorities related to the selection of materials, manufacturing, use and disposal of our products, and the needs and concerns of people in the adidas value chain. Finally, we see an alignment with SDG 17 on Partnerships as we are strongly committed to collaborating with our industry partners and all other levels of society to find long-lasting solutions to global environmental and social challenges.

## CORRELATION BETWEEN UN SDGS AND OUR SUSTAINABILITY ROADMAP



## 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 Zero Discharge of Hazardous Chemicals (ZDHC) working group, 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), the Bangladesh Accord on Fire and Building Safety 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 International Labour Organization's (ILO) Better Factories program in Cambodia. As an active participant in the Bali Process Government and Business Forum we have formally endorsed our commitment to the Acknowledge, Act, Advance Recommendations, that outline actions to advance long-term efforts to improve supply chain transparency, the treatment of workers, and ethical recruitment. [➔ 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 we disclose the names of factories of suppliers who process materials for our primary suppliers or sub-contractors, 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 the programs that drive achievement of our voluntarily set goals for 2020. A Sponsor Board composed of functional heads and senior representatives 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

▣ adidas continuously receives positive recognition from international institutions, rating agencies, NGOs and socially responsible investment analysts for our sustainability initiatives. In 2018, the company was again represented in a variety of high-profile sustainability indices and subject to comprehensive corporate sustainability assessments.

[▣ SEE OUR SHARE, P. 57](#)

For the 19th consecutive time, adidas 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. adidas was assessed for its corporate economic, environmental and social performance and rated as overall leader in the Textiles, Apparel and Luxury Goods Industry, receiving industry-best scores in seven criteria: Innovation Management, Materiality, Supply Chain Management, Human Rights, Environmental Policy and Management Systems, Operational Eco-Efficiency and Social Reporting. As a result of our response to the Carbon Disclosure Project (CDP) in 2018, adidas was again awarded with a B score in the Climate Change submission (2017: B) and with a B- score in the Water submission (2017: A-). The company continued to be positioned among the top ten in the leather and textiles industry in the annual Green Supply Chain Corporate

Information Transparency Index (CITI), which forms the first quantitative evaluation system designed to assess brands' environmental management of their supply chains in China. adidas also improved its score to top the Corporate Human Rights Benchmark (CHRB) evaluation in 2018, coming in first overall, with more than 100 companies across various industries assessed against the CHRB's criteria of human rights performance. The company scored particularly well in criteria such as 'Embedding Respect and Human Rights Due Diligence', 'Remedies and Grievance Mechanisms' as well as 'Performance: Responses to Serious Allegations'. [▣](#)

[➔ ADIDAS-GROUP.COM/S/RECOGNITION](https://www.adidas-group.com/s/recognition)

## OUR PROGRESS

Following our ambition to be transparent toward our stakeholders, for years, adidas has regularly reported about its sustainability performance by measuring and disclosing the progress made toward our targets. The following presents the list of material topics within our programs and details the progress made and challenges faced in 2018.

## PRODUCT SAFETY AND TRANSPARENCY

▣ 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.

[➔ ADIDAS-GROUP.COM/S/PRODUCT-SAFETY](https://www.adidas-group.com/s/product-safety)

In 1998, adidas pioneered the Restricted Substances Policy ('A-01' Policy). The 'A-01' Policy 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 and published internally and externally at least once a year based on findings in our ongoing dialogue with scientific organizations, and it is mandatory for all business partners, who have to confirm receipt and acknowledgement of the latest policy update each year in a written format.

To ensure successful application of the policy, we monitor and influence standards and regulations through external observation and interaction, promote internal business understanding and offer global support by developing guidelines and systems. One example is our 'Product Safety and Compliance' workspace on our global intranet a-LIVE. It 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 follow national and international regulations and best-practice standards as well as are in accordance with the laws of intellectual property. Both our own quality assurance laboratories and external testing institutes are used to constantly monitor material samples to ensure supplier compliance with our requirements, with the aim to efficiently manage product safety and avoid any product recalls. Materials that do not meet our standards and specifications are rejected. Senior management from Social and Environmental Affairs as well as Global Operations reviews and signs off policy updates and is informed about proper execution and monitoring.

One of the recent results of our ongoing collaboration with the AFIRM Group was the creation of a consolidated AFIRM Restricted Substances List that harmonizes Restricted Substances Lists across the industry. We co-hosted the AFIRM Group RSL summit with more than 400 participants in Vietnam

in 2018 to inform about the latest updates and drive the agenda of a global best-practice industry approach. We further continued our participation in public stakeholder consultation processes initiated by the European Commission (e.g. ECHA) and US state legislative initiatives to inform governmental entities on implications and opportunities of drafted legislation.

In 2018, adidas announced a voluntary recall of children's swimwear products in the Infinetex 3-Stripe range after having received customer reports about a potential unexpected peeling off of the three stripes on swimwear in this range when in contact with water. A subsequent third-party investigation showed that using the affected swimwear products could pose a potential safety risk to children as the stripes might get caught on objects or other children and become entangled, potentially leading to injuries. Sales of affected swimwear products in all sizes were stopped immediately, which was supported by communication on both

our corporate website and e-com website. No injuries have been reported to us to date. [↩](#)

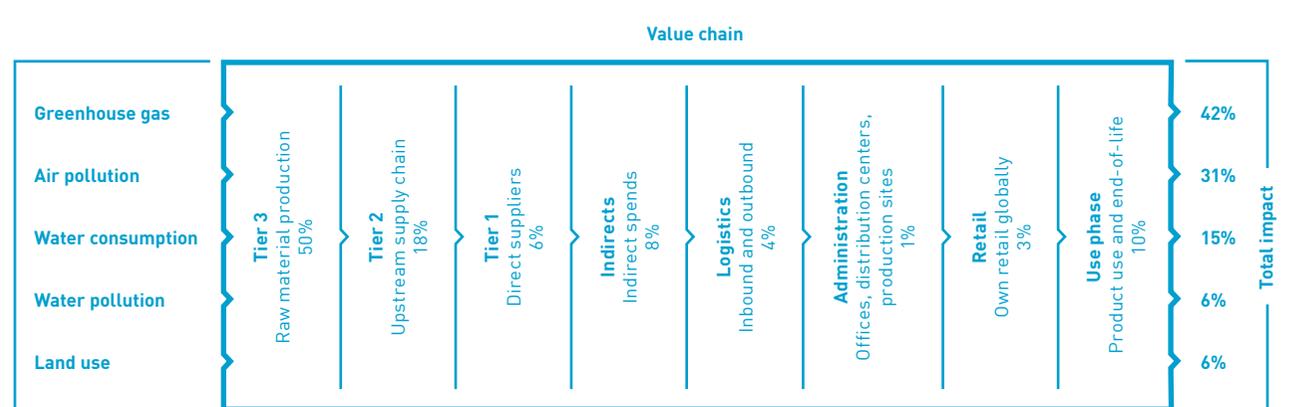
**ENVIRONMENTAL IMPACTS**

Managing the environmental impacts at our own sites and along the value chain is a key focus of our work. We have developed an approach to address water efficiency and quality and are committed to steadily increasing the use of more sustainable materials in our production, products and stores while driving toward closed-loop solutions. We are committed to reducing our absolute energy consumption and CO<sub>2</sub> emissions, transitioning to clean energy and looking into energy-harvesting opportunities.

In 2016, for the first time, we conducted a fact-based pilot analysis to assess our organizational environmental footprint.

SEE DIAGRAM 37 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

Organizational footprint<sup>1</sup>



<sup>1</sup> Greenhouse gas: carbon dioxide, methane and nitrous oxide. Air pollution: i.a. 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.



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, that means 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. We are using the results for the further evolution of our sustainability strategy and programs, and in 2018 we looked into options to further develop the methodology, with the aim to repeat this analysis.

In addition to responding to climate change through tailored programs that improve the environmental footprint in our own operations and in the supply chain, adidas is proactively addressing the impacts of climate change through various partnerships. The company joined the 'UN Climate Neutral Now' initiative in 2015 and committed to action steps as a champion of the initiative, such as the continued estimation and reduction of its emissions. In 2018, adidas reinforced its support to accelerate the transformative change needed to reach greenhouse gas emission neutrality in the second half of the 21st century by joining the 'UN Fashion Industry Charter for Climate Action'. The initiative will build a roadmap for the industry to deliver the goals from the Paris Agreement. As a participant, adidas commits to the target of achieving a 30% reduction in GHG emissions by 2030, aiming to build the way toward carbon neutrality by 2050.

### Own sites

Since 2008, the adidas 'Green Company' program strives to achieve ambitious savings in water, waste and energy at adidas own sites globally. The program includes administrative offices, production facilities and distribution centers, and covered more than 90% of our global employee base (excluding own retail) in 2018. In 2015, we presented a set of targets to be

achieved by 2020, including targets for carbon emissions reduction that were calculated considering a science-based methodology and context-based targets for water reduction.

[➔ ADIDAS-GROUP.COM/S/ENVIRONMENTAL-APPROACH](https://www.adidas-group.com/s/environmental-approach)

In 2018, despite an increased number of sites considered in our reporting, we achieved an accumulated reduction of 24% in combined carbon net emissions (baseline 2015). This is the result of the implementation of ambitious energy efficiency programs, the use of carbon offsetting for key locations in Europe, as well as the introduction of real-time monitoring of performance in key locations that enable us to react fast if performance is not on track. We also managed to improve water efficiency at our sites, which is mainly due to increased awareness of our employees. Between 2008 and 2018, we saw a 31% accumulated reduction in water consumption per employee. [■ SEE TABLE 38](#)

To support the achievement of our Green Company targets, we have implemented an Integrated Management System (IMS) that combines three existing management systems for environment (ISO 14001), energy (ISO 50001), as well as health and safety (OHSAS 18001). The IMS helps us to drive further business integration and take impact-relevant decisions for our operations globally. A dedicated IMS policy ensures solid application among all adidas entities affected, and our global intranet a-LIVE enables best-practice sharing among all

employees. We aim to continuously expand certifications to key sites and prepare them to pass the external certification process by conducting regular internal audits. By the end of 2018, a total of 20 sites held an ISO 14001 certification (2017: 17), including our headquarter offices in Herzogenaurach and Portland, our offices in Amsterdam, Boston, Panama, Shanghai and Tokyo, as well as our distribution centers in Germany, Indianapolis/USA and Brantford/Canada.

In 2017, the adidas Executive Board 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. By now, the majority of facilities managed to phase out single-use plastics where possible. Single-use plastic might, however, still be in use where not replaceable, e.g. for hygiene reasons. The announcement that was made on our global intranet a-LIVE was one of the most successful posts to date, showing the high commitment and engagement of both our Executive Board and employees worldwide toward responsible business practices.

The progress toward all Green Company targets is tracked through an environmental data reporting system and is disclosed in detail in our annual 'Green Company Report' that will be available on our corporate website as of April 2019.

[➔ ADIDAS-GROUP.COM/S/ENVIRONMENTAL-APPROACH](https://www.adidas-group.com/s/environmental-approach)

### Own sites: Progress toward 2020 targets

38

2020 Targets	2018	2017	2016	
<b>Emissions</b>	3% absolute annual reduction in CO <sub>2</sub> Scope 1 and Scope 2 net emissions <sup>1</sup> (baseline 2015)	(24%)	(29%)	(11%)
<b>Water</b>	35% reduction in water consumption per employee (baseline 2008)	(31%)	(27%)	(23%)

<sup>1</sup> 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.

## 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 adidas, sourcing is not only about ensuring high product quality and timely delivery, it also means working with our suppliers to ensure they are able to continuously improve their environmental footprint. We do so by providing them with policies and best-practice guidance for environmental management, by offering training sessions tailored to their needs, and by measuring their progress toward clear reduction targets we expect them to achieve by 2020. [SEE TABLE 39](#) Progress toward these targets is regularly reported to senior management for review and further decisions.

Using the environmental performance of adidas own sites as best-practice examples, we provide a set of specific mandatory policies and guidelines to our suppliers. The adidas 'Workplace Standards' (the supply chain code of conduct) as well as supportive guidelines such as our 'Environmental Guidelines' are updated regularly and build the basis for our engagement with suppliers. In 2018, we released a newly developed 'Environmental Good Practice Guide and Toolkit' to our suppliers. The guide serves as a manual to recommend good industry practices for reducing environmental impacts of manufacturing facility operations. It outlines the adidas approach to the implementation of Environmental Management Systems, data management, wastewater management, and Green Building Management, and provides over 60 saving opportunities on energy, water, and waste management and renewable energy.

adidas has initiated a system of multi-level and cross-functional training sessions with its global supplier network. We undertake several steps to support and to ensure

suppliers' performance is on track to achieve their 2020 targets. [SEE TABLE 39](#) In 2018, we continued to support a couple of initiatives to accelerate suppliers' target achievement. We started the 'Energy and Water Investment Plan' project with facilities located in five of our main sourcing locations (Cambodia, China, Indonesia, Vietnam and Taiwan) that were off track to achieve their targets, or that were recently added to the scope of our monitoring. These facilities are required to conduct on-site assessments and develop an investment plan enabling them to deliver on their energy and water reduction targets, with the aim to identify potential efficiency measures and achieve actual savings by implementing these saving opportunities on-site before the end of 2019. We also saw the successful completion of an 18-month 'Energy and Water Efficiency' project that we co-funded together with the International Finance Corporation (IFC) and which benefited six supplier facilities in Vietnam. The aim of this partnership was to provide access to advisory services as well as low-cost financing for suppliers who wish to invest in improving their energy and water footprint but need technical support or the upfront capital to do so. Since the start of the project in 2017, suppliers have implemented more than 60 saving opportunities, with notable annual

savings in energy consumption, greenhouse gas emissions and water consumption. As part of the project with the IFC, we conducted a renewable energy assessment, identifying those suppliers with the feasibility of using renewable energy.

We set ambitious reduction intensity targets for our strategic suppliers<sup>1</sup> at Tier 1 and Tier 2 level, aiming to systematically improve their environmental performance. By 2020, we expect them to reduce their overall energy consumption, water use and waste volume by 20% compared to their performance in 2014. We also set a 35% target for reduction in water use for our strategic apparel material suppliers<sup>2</sup> at Tier 2 level. 2018 results show the promising efforts we are putting into driving resource efficiency. Suppliers are on track to meet their 2020 reduction targets across all categories (footwear, apparel, and accessories and gear), with overachievers compensating low performers in the aggregated reduction results.

[SEE TABLE 39](#)

A tool called 'E-KPI' helps us to measure suppliers' environmental compliance overall and assess their performance and progress toward the 2020 targets. Using a benchmarking approach, the E-KPI allows for a high level of

### Supply chain: Progress toward 2020 targets

39

2020 Targets <sup>1</sup>		2018	2017	2016
Water	20% reduction in water consumption at strategic Tier 1 supplier facilities	(24%)	(15%)	(11%)
	35% reduction in water consumption at strategic Tier 2 apparel material supplier facilities	(27%)	(24%)	(7%)
Energy	20% reduction in energy consumption at strategic Tier 1 supplier facilities and strategic Tier 2 apparel material supplier facilities	(15%)	(7%)	(9%)
Waste	20% reduction in waste volume at strategic Tier 1 supplier facilities and strategic Tier 2 apparel material supplier facilities	(22%)	(10%)	(4%)

<sup>1</sup> Aggregated reduction results for suppliers with 2014 baseline in all categories (apparel, footwear and accessories and gear). Externally verified data for the previous year.

<sup>1</sup> Strategic suppliers account for around 75% of all production volume.

<sup>2</sup> Apparel material suppliers are specialists in printing and dyeing operations. Based on results from previous years and a change in our tracking methodology, in 2017 the target for our apparel material suppliers was adjusted to a 35% reduction by 2020.

transparency into suppliers' actual consumption intensity, hence supporting us in defining suppliers' specified areas for improvement and training needs that match their respective situation. We will continue to support suppliers to identify resource efficiency measures and rollout in our supply chain.

An additional way 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, 98% (2017: 95%), 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.

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. 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 around 11 grams in 2018.

**Chemical management:** The management of chemicals in multi-tiered supply chains is a complex challenge and requires many actors contributing to the achievement of effective and sustainable solutions. For years, adidas has been running leadership programs in Chemical Management within its area of direct influence. In consultation with external stakeholders including chemical experts, environmental organizations and industry federations, adidas has defined an end-to-end-approach spanning the management of chemical input, monitoring supplier progress and reporting supplier data publicly to controlling the finished end product. Our

approach was reviewed by the Sponsor Board and approved by SEA and GOPS senior management.

Our targets for 2020 include achieving 100% sustainable input chemistry by means of adopting the ZDHC Manufacturing Restricted Substances List (MRSL), phasing out hazardous chemicals and providing our strategic suppliers with a list of positive chemistry (the bluesign bluefinder).

[ADIDAS-GROUP.COM/S/CHEMICAL-FOOTPRINT](https://www.adidas-group.com/s/chemical-footprint)

In 2018, we analyzed the feedback of our suppliers on the MRSL acknowledgement letters and now aim to build an automated system to monitor and track supplier compliance with the MRSL. Starting in 2019, we will run a pilot with the majority of our strategic apparel material suppliers at Tier 2 level that will help us to define an MRSL monitoring and tracking strategy. We contributed to the ZDHC Wastewater Guidelines, an international wastewater standard officially released in 2016, and put further efforts into the elimination of hazardous chemicals from the production processes by strengthening our wastewater monitoring approach and adopting the ZDHC Wastewater Guidelines. Following these guidelines, our suppliers are required to test and publicly report their wastewater test results on the ZDHC Wastewater Gateway twice a year. After piloting the reporting in 2017, suppliers accounting for more than 80% of the wet processes reported their data in 2018. We made progress toward the

**Products free of PFC**

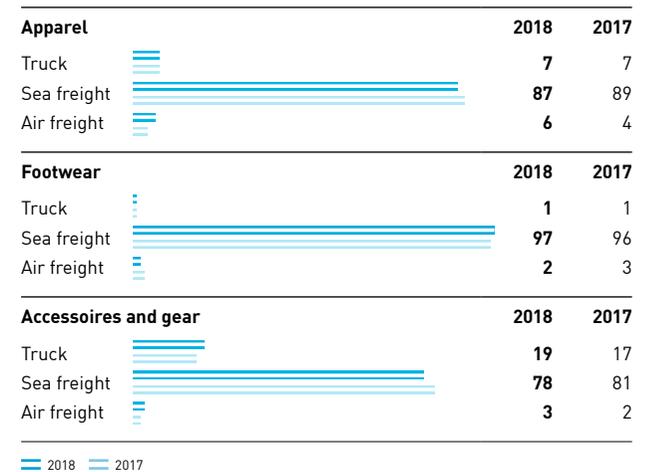


2020 target to have 80% of auxiliaries and 90% of dyestuffs bluesign-approved, recording 76% of auxiliaries and 87% of dyestuffs from our strategic apparel suppliers as bluesign-approved by the end of 2018. We also met the target to uphold our commitment of being more than 99% free of poly- and perfluorinated substances (PFCs) in our products for the fall/winter 2019 season.

**Transportation**

In 2018, we tracked again the environmental impact related to the transport of our goods. Compared to the previous year, performance remained relatively stable with major changes being a slight increase in sea freight for footwear products and a slight increase in air freight for apparel products and accessories and gear. The vast majority takes place via sea freight. [SEE DIAGRAM 40](#)

**Freight types used to ship adidas and Reebok products<sup>1</sup> in % of products shipped** 40



<sup>1</sup> 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

▮ 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 is tracked and managed by the respective materials development and sourcing departments, progress toward targets is reported to senior management for review and further decision.

We are aware that products made out of synthetic fiber can cause negative environmental impacts during their use phase. We acknowledge microfiber pollution as a complex challenge for our industry, and are proactively addressing the problem. To foster collaboration and drive joint action toward further improvements, in 2018, for example, we hosted a two-day microfiber industry summit to which we invited experts from institutes, academia, NGOs, industry associations and other brands to create awareness and drive harmonization, especially with a focus on a global harmonized testing standard. [➔ ADIDAS-GROUP.COM/S/PRODUCT-MATERIALS](https://www.adidas-group.com/s/product-materials)

### Sustainable cotton

As a founding member of the Better Cotton Initiative (BCI), adidas is working to reduce the use of conventional cotton and **Sustainable cotton sourced** has committed to increasing the sourcing volumes of Better Cotton, with the aim of achieving 100% **sustainable cotton** [▮ SEE GLOSSARY](#) by 2018. BCI aims to reduce the use of pesticides, promotes efficient water use, crop rotation and fair working conditions, and strives to transform cotton production worldwide by developing Better Cotton as a sustainable mainstream commodity. Not only was this objective met, but adidas is a frontrunner in reaching its intended target. In 2018, 100% (2017: 93%) of the cotton we sourced globally was sustainable cotton<sup>3</sup>. 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.

### Recycled polyester

Recycled polyester is a synthetic fiber based on post-consumer waste, such as plastic bottles and used garments. The raw material is reprocessed and spun into fibers. Using recycled polyester has many benefits over virgin polyester. It helps us to reduce our dependency on non-renewable petroleum and decreases our carbon impact when compared to conventional polyester. Polyester is the most used material in adidas products, and using more recycled polyester is one way we seek to improve our environmental footprint while still making high-performance products for the athlete.

We aim to replace all virgin polyester with recycled polyester in all adidas and Reebok products where a solution exists by 2024. We have set clear internal milestones for our product creation teams and have tracked a steady increase in the use

of recycled polyester in our adidas and Reebok products throughout the last seasons.

### Parley Ocean Plastic

Since 2015, adidas has partnered up with *Parley for the Oceans* [▮ SEE GLOSSARY](#), an environmental organization and global collaboration network. 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. We aim to avoid the use of plastic in our own operations, are working to prevent plastic from entering the oceans and are using *Parley Ocean Plastic* [▮ SEE GLOSSARY](#) as an eco-innovative replacement for virgin plastic. We are driving eco-innovation around materials and products, and new ways of using them, with the ultimate goal of reinventing current plastic and instead transforming it into performance sportswear.

In 2018, we continued to roll out Parley Ocean Plastic across our key categories and were able to exceed our target, with **Shoes containing Parley Ocean Plastic** [▮ SEE GLOSSARY](#) more than five million pairs of shoes containing Parley Ocean Plastic made. To facilitate the growing demand for Parley Ocean Plastic and other sustainable materials, we have built a dedicated sourcing operation with the aim to ensure a steady and transparent supply chain. Together with Parley for the Oceans, we developed a code of conduct specific to the collection and processing of plastic, that is now applied by our selected partners operating in countries in scope.

[▮ SEE GLOBAL OPERATIONS, P. 74](#), [▮ SEE ADIDAS BRAND STRATEGY, P. 67](#), [▮ SEE INNOVATION, P. 78](#), [➔ ADIDAS-GROUP.COM/S/SUSTAINABILITY-INNOVATION](https://www.adidas-group.com/s/sustainability-innovation)

100%

> 5m

<sup>3</sup> 99% of all cotton volume was sourced according to the Standards of the Better Cotton Initiative, around 1% was sourced as organic cotton and 0.03% was sourced as conventional cotton.

### Waste and packaging

Our commitment to reducing our plastic footprint has already resulted in some tangible outcomes, such as the phase-out of plastic bags in our own retail stores globally already in 2016 and the elimination of single-use plastics across the majority of adidas locations worldwide. Where the use of plastics – for example in transport packaging – is still unavoidable, adidas is relying on counterbalancing measures and promoting sustainable alternatives. In 2018, the company supported the global innovation platform Fashion for Good with a donation of € 1.5 million which equates to the company's environmental impact of plastic packaging. The foundation is driving the development of innovative, durable and reusable materials for the fashion industry. adidas has been a partner of the foundation since the beginning of 2018.

### Take-back programs

In 2018, we rolled out our global take-back program to nine stores in some of our selected key cities (London, Paris, New York and Los Angeles) and markets, with the main objective to raise consumers' awareness of what happens to products at the end of their 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 5%) cannot be recycled and thus is sent for disposal. [➤ ADIDAS-GROUP.COM/S/PRODUCT-END-OF-LIFE](https://www.adidas-group.com/s/product-end-of-life)

### Water treatment technologies

In 2018, we continued to look into different technologies 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. **▬**

### APPROACH TO HUMAN RIGHTS

adidas recognizes its responsibility to respect, protect and promote human rights and the importance of showing that we are taking the necessary steps to fulfill this 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. 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.

[➤ ADIDAS-GROUP.COM/S/HUMAN-RIGHTS](https://www.adidas-group.com/s/human-rights)

Throughout 2018, we engaged with a broad spectrum of human and labor rights advocacy groups, working collaboratively with the FLA in calling for the Cambodian government to address freedom of expression and association, including support for the continued operation of Cambodia's Arbitration Council, which handles labor disputes. We benchmarked our current sourcing practices in Myanmar against the recommendations of the UN-backed Fact-Finding Mission on Myanmar. Together with other stakeholders, we have maintained a seat on FIFA's Independent Advisor Board on Human Rights, providing input and recommendations to FIFA on the hosting of the 2018 Russia World Cup. Finally, we have continued to support the Business Network for Civic Freedoms and Human Rights Defenders (HRDs) and contributed to guidance published on the role of business in protecting HRDs.

As part of its human rights efforts, adidas developed a modern slavery outreach program that looks beyond strategic suppliers on Tier 1 level, seeking to gain greater transparency in its supply chain. In 2018 we continued our efforts to tackle modern

slavery risks in our upstream supply chain, targeting the areas that fall outside of our mainstream auditing activities. Examples range from providing targeted modern slavery training to 1,800 frontline Sourcing and Procurement employees globally to engaging with our suppliers on Tier 2 level across key sourcing countries in Asia on identifying and remediating non-socially responsible practices. We have directed our efforts at raw material suppliers for natural rubber at Tier 3 level and are part of an FLA multi-stakeholder project to investigate risks in the natural rubber supply chain in Vietnam. To strengthen our commitment to the responsible recruitment and treatment of migrant labor, we engaged in a **KnowTheChain** project with the International Organization for Migration focused on specific high-risk migrant corridors in Asia. Our efforts have been recognized in the KnowTheChain 2018 benchmarking for addressing forced labor risks, with adidas ranking first out of the 44 apparel and footwear companies that were part of the assessment. **▬**

### WORKING CONDITIONS IN OUR SUPPLY CHAIN

Core to the human rights approach of adidas is its commitment to ensuring fair labor practices, fair compensation and safe working conditions in factories throughout its global supply chain. Our active efforts are guided by the adidas 'Workplace Standards', our supply chain code of conduct. The standards form a contractual obligation under the manufacturing agreements adidas signs with its main business partners to provide provisions for workers' health and safety and ensure environmentally sound factory operations, 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



1<sup>st</sup> place

and approves all policies and implementation processes of the labor rights program.

adidas regularly rates suppliers on their ability to deliver fair, healthy and environmentally sound workplace conditions by means of conducting announced and unannounced audits through adidas personnel or an approved external auditor. We use a KPI rating system for social compliance (C-KPI) and attach scores between 1 and 5, with 1 being the worst and 5 being the best. According to the results, our sourcing teams decide the course of action, ranging from the definition of training needs at the factories to reinforcement mechanisms such as sending warning letters or even termination of contracts.

Any cases of non-compliance identified during audits are given a certain time frame for remediation. Potential new suppliers are assessed in a similar way and orders can only be placed if approval by the SEA team has been granted. adidas operates several grievance channels allowing workers or third parties to submit complaints about violations of the Workplace Standards or human rights generally. All complaints are reviewed and investigated, and the outcome is reported on our website. Factory conditions are also inspected by independent auditors through our participation in the Fair Labor Association, which we joined as a founding member in 1999. We are committed to independent and unannounced factory inspections and external verification of our programs.

At the end of 2018, adidas worked with 684 independent supplier facilities<sup>4</sup> (2017: 782) who manufacture products for our company in 51 countries (2017: 56). The fall in the number of facilities is due to further consolidation of our supply chain and local sourcing integration under Global Operations. We worked with 64 licensees whose suppliers manufactured products in 375 factories across 41 countries (2017: 62 licensees in 360 factories across 44 countries). More than 70% of the factories are located in the Asia-Pacific region.

### Onboarding

In 2018, we conducted initial assessments (IA), the first approval stage for new entry factories, in 221 factories (2017: 209). The total number increased by around 5% compared to 2017, mainly due to our decision to extend our IA monitoring coverage to suppliers at Tier 2 level. 55 factories (2017: 50 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 41](#) 90% of all initial assessments were undertaken in Asia (2017: 81%), with China accounting for 41% of these assessments (2017: 42%).

Overall, at the end of 2018, the 'first-time rejection rate' of 30% of all new factories visited was similar to the previous year (2017: 29%) and the 'final rejection rate' was at 3% (2017: 2%). [SEE TABLE 41](#) 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

### Worldwide rejections after initial assessment due to compliance problems

41

	2018	2017
Total number of first-time rejections <sup>1</sup>	55	50
First-time rejection rate	30%	29%
Total number of final rejections <sup>2</sup>	5	4
Final rejection rate	3%	2%

<sup>1</sup> 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.

<sup>2</sup> 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.

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 and results in 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 acceptance.

### Visits and training

During 2018, 546 factory visits (2017: 226) were undertaken. The considerable increase in visits was linked to our engagement with factories to improve working conditions, and our efforts to empower workers through several targeted projects. These visits involved various types of monitoring, suggestions for sustainable remediation, and project meetings with factory management.

<sup>4</sup> Independent supplier facilities refer to individual Tier 1 facilities (factories) of our manufacturing partners (suppliers) that adidas has a manufacturing agreement with, and their Tier 2 subcontractor facilities, excluding own factories and licensee facilities. Facilities that work with our licensees are reported separately. Some of these facilities may produce both for adidas directly and for licensee.

Number of training sessions by region and type<sup>1</sup>

42

Region	Type and number of training sessions							
	Fundamental <sup>2</sup>		Performance <sup>3</sup>		Sustainability <sup>4</sup>		Total	
	2018	2017	2018	2017	2018	2017	2018	2017
Asia	31	42	13	4	15	49	59	95
Americas	55	24	2	0	10	1	67	25
EMEA	12	7	4	2	1	3	17	12
<b>Total</b>	<b>98</b>	<b>73</b>	<b>19</b>	<b>6</b>	<b>26</b>	<b>53</b>	<b>143</b>	<b>132</b>
In %	69	55	13	5	18	40	100	100

<sup>1</sup> Training sessions conducted for suppliers, workers, licensees, agents and adidas employees.

<sup>2</sup> Fundamental training covers Workplace Standards and SEA introduction, FFC training as well as SEA policies and standard operating procedures.

<sup>3</sup> Performance training covers specific labor, health, safety and environmental issues.

<sup>4</sup> Sustainability training covers management systems and KPI improvements as well as factories' internal monitoring programs.

Additionally, we conducted 143 training sessions and workshops for suppliers, licensees, workers and adidas employees (2017: 132). The 8% increase in the number of training sessions is aligned with the increase in the number of visits, to support and enable the suppliers to improve their workplace conditions and environmental performance. In total, 1,282 people (2017: 1,907) attended the training sessions, which mainly covered fundamental topics, and which were executed within smaller groups. ■■ SEE TABLE 42

### Worker empowerment

In parallel to our existing grievance systems such as anonymous local language-based worker hotlines, we implemented additional digital tools that enable workers to ask questions and raise concerns directly with their employers. Following the successful piloting of an innovative 'SMS Worker Hotline' back in 2012, we have progressively improved our suppliers' operational grievance mechanisms, using an application-based 'Workers Voice' platform that was available and used in 97% of our strategic factories across ten countries by the end of 2018. ■■ SEE TABLE 43

### Grievance application

43

2020 Target	2018	2017	2016
Implementation of 'Workers Voice' Grievance Platform at strategic suppliers: 100%	97%	63%	58%

The top three types of complaints in 2018 were related to the categories of benefits, personal issues and working hours. Responses received through this platform are carefully tracked and help us understand the main challenges and worker rights issues faced by workers in the factories, ultimately allowing us to monitor how the factory management teams find solutions and communicate back to their workers.

Complementing the various grievance channels, we measure the level of worker satisfaction through annual in-factory surveys. The survey results are shared with auditors and the factory management and offer insights into worker concerns, as well as potential areas for workplace improvement. By the

end of 2018, worker satisfaction surveys were conducted in 123 supplier factories in twelve countries (2017: 47 factories across nine countries). Upon completing the survey, factories are required to develop improvement plans for the 'top three' issues and then track progress regularly. Based on the feedback captured by the surveys we have seen, for example, constructional improvements in canteens and worker dormitories as well as a positive drive to develop better training programs for workers and supervisors.

Alongside factory-led training, adidas has also offered tailored training for supervisors since 2016. Up until the end of 2018, more than 700 supervisors in 55 factories across five countries received such training. Supervisors have shown a strong commitment to the training courses and post-event assessments. And we have received very positive feedback from trainers and factory management regarding the supervisors' improved work performance. As part of our larger efforts to empower female workers in our supply chain, we initiated a 'Women's Empowerment Program' in Pakistan to train women on how to secure better career opportunities in the workplace. Since its start in 2015, the program has benefited more than 400 on-job women as well as women workers made redundant.

### Monitoring

We audit our suppliers regularly against our Workplace Standards. In 2018, a total of 1,207 social compliance audits and environmental assessments (2017: 1,015) were conducted. Performance audits at our current suppliers dropped by 10%, which is in line with the decrease in the number of suppliers.

Number of audits by region and type

44

Region	Initial assessment <sup>1</sup>		Performance audit <sup>2</sup>		Environmental assessment <sup>3</sup>		Total	
	2018	2017	2018	2017	2018	2017	2018	2017
	Asia	198	170	479	544	379	138	1,056
Americas	14	9	64	70	16	12	94	91
EMEA	9	30	43	37	5	5	57	72
<b>Total<sup>4</sup></b>	<b>221</b>	<b>209</b>	<b>586</b>	<b>651</b>	<b>400</b>	<b>155</b>	<b>1,207</b>	<b>1,015</b>

<sup>1</sup> Every new 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.  
<sup>2</sup> Audits conducted in approved factories that have passed the initial assessment.  
<sup>3</sup> Includes environmental assessments and SAC HIGG data verification. 2018 figures also include wastewater test assessments according to the ZDHC Wastewater Guidelines.  
<sup>4</sup> Includes audits done in licensee factories.

The total number of environmental assessments increased notably compared to the previous year, as a result of additional wastewater tests carried out in accordance with the ZDHC Wastewater Guidelines in 2018. [SEE TABLE 44](#) In addition, 102 self-governance audits and collaboration audits were conducted (2017: 114). When a factory reaches a compliance maturity level of 4C and above, we empower the supplier to conduct their own self-governance audits and develop appropriate remediation plans, which we periodically review. Collaboration audits are conducted in partnership with other brands, or as part of joint remediation exercises.

The number of audits in factories manufacturing goods for licensees increased slightly by 3% compared to 2017, up to 323 in 2018, in line with the increase in percent we have seen in the number of licensees, from 62 in 2017 to 64 in 2018. The number of self-governance and collaboration audits at licensee factories totaled 19 at the end of 2018 (2017: 26).

The number of audits using in-house technical staff decreased to 354 (2017: 409), while audits conducted by third-party monitors commissioned by suppliers, adidas business units

and licensees increased to 620 at the end of 2018 (2017: 606). In addition, 233 test assessments according to the ZDHC Wastewater Guidelines were conducted.

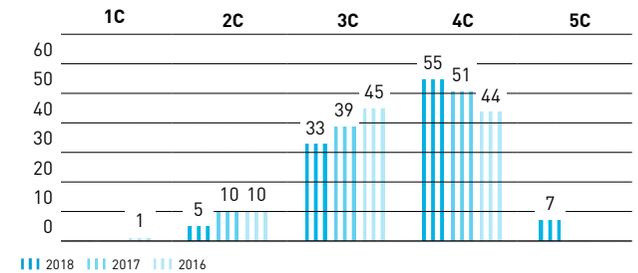
A total of 47% (2017: 48%) of all direct and licensee facilities were audited in 2018. 'High-risk' locations in Asia<sup>5</sup>, the major sourcing region of adidas, received extensive monitoring in 2018 with an audit coverage that was close to 65% (2017: 70%). As a general principle, factories located in low-risk countries (i.e. with strong government enforcement and inspectorate systems) are considered out of scope for our audit coverage.

Our audits help us rate our suppliers according to their social and environmental compliance performance with a C-KPI and E-KPI rating tool, respectively. An evaluation of E-KPI is contained in the description of the environmental performance of our supply chain.

In 2018, almost two-thirds of our strategic factories<sup>6</sup> achieved a rating of 4C or better, compared to 31% in all direct factories, indicating that strategic factories have achieved much more

Social compliance performance rating of strategic supplier factories by C-KPI rating

45



advanced compliance levels. Additionally, 7% of our strategic factories have achieved 5C rating, indicating that they have mature social compliance systems and practices in place.

[SEE DIAGRAM 45](#), [SEE TABLE 46](#)

Of our strategic licensee factories, 80% successfully embedded governance systems, supply chain management, purchasing practices and product safety compliance requirements into their business practices. 20% achieved a 'Sustainability Leadership' level, signaling that in addition to achieving high scores in other sections, they also scored above 80% in the sustainability section of the Report Card, which measures the existence of policies and implementation, stakeholder engagement, public reporting and communication. [SEE TABLE 46](#)

Non-compliances identified 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

<sup>5</sup> 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.  
<sup>6</sup> In 2018 we changed from reporting detailed C-KPI performance of direct suppliers to reporting C-KPI performance of strategic suppliers. Strategic suppliers account for around 75% of all production volume.



Supply chain: Progress toward 2020 targets

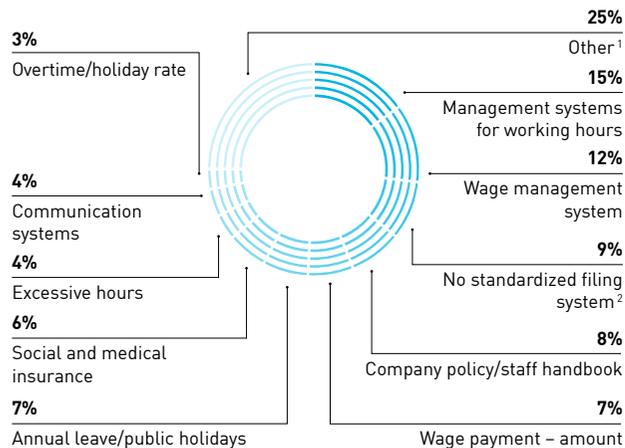
46

2020 Targets		2018	2017	2016
Strategic Tier 1 suppliers <sup>1</sup>	80% to reach at least 4C rating	62%	50%	17%
	10% to reach 5C rating	7%	0	0
Strategic licensees	80% to achieve 80% or above in Score Card reports	80%	55%	50%
	10% to achieve Sustainability Leadership	20%	0	0

<sup>1</sup> Strategic suppliers are responsible for around 75% of all production volume.

Top 10 labor non-compliance findings identified during audits in 2018

47

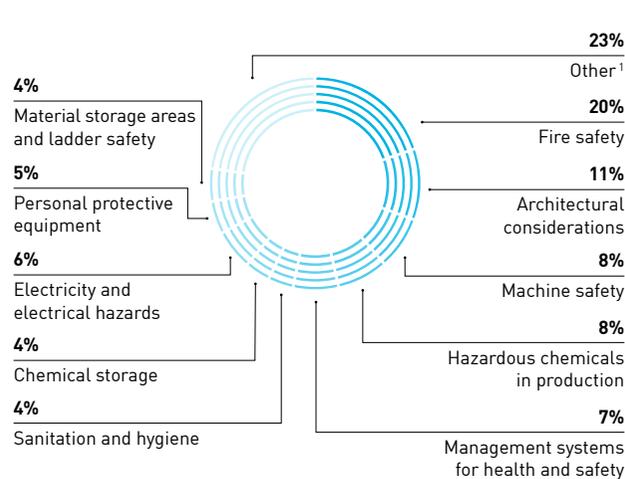


<sup>1</sup> 'Other' includes, for example, freedom of association issues, and management system for disciplinary practices.

<sup>2</sup> '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 2018

48



<sup>1</sup> 'Other' includes, for example, housekeeping, occupational hazard risk assessment, and ergonomics.

life-threatening health, safety and environment conditions – immediately trigger a warning and potential disqualification of a supplier. We report these non-compliance findings that were identified through performance audits, collaboration audits and self-governance assessments in 2018. We follow

up on all cases of non-compliances and seek to remediate them within a given timeframe.

– **Labor non-compliances:** Besides identifying non-compliances with our Workplace Standards, the 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 47](#)

– **Health and safety non-compliances:** Fire, electrical and machine safety are critical areas for existing suppliers and together accounted for 34% of the non-compliances identified in 2018. The way chemicals were stored and used, including the presence of banned chemicals, accounted for 12% of non-compliance findings reported. A further 7% 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 48](#)

Independent FLA audits

In 2018, the FLA conducted three factory assessments or remediation verification exercises (2017: 4) 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 2018, adidas completed four of these redirect activities (2017: 12) on the topics of, for example, fair compensation and activities beyond our Tier 1 level, including traceability of the rubber supply chain in Vietnam, mapping and traceability of cotton in Turkey, and giving subcontracting guidance.

In 2017, the FLA accredited the adidas program for the third time. The accreditation recognized adidas' leadership to coordinate brand efforts, which address labor violations, and included commendation for the application of mobile technology to implement a 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.

### 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 2018, we had a total of 39 active warning letters (2017: 42) across 16 countries. The largest number of warning letters continues to be issued in Asia, where more than 70% of all supplier factories are located. Compared to the previous year, the overall number of active first warning letters decreased slightly as did the total number of second warnings, with one letter being issued (2017: 3). 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) remained stable in 2018 (2017: 1). [SEE TABLE 49](#) 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 2018 included non-compliance in regard to fire safety practices, receipt of

### Number of warning letters by region<sup>1</sup>

49

Region	1st warning		2nd warning		3rd and final warning		Total warning letters	
	2018	2017	2018	2017	2018	2017	2018	2017
Asia	30	35	1	1	1	0	32	36
Americas	5	2	0	1	0	0	5	3
EMEA	2	1	0	1	0	1	2	3
<b>Total</b>	<b>37</b>	<b>38</b>	<b>1</b>	<b>3</b>	<b>1</b>	<b>1</b>	<b>39</b>	<b>42</b>

<sup>1</sup> Includes warning letters issued by licensees and agents, but excluding warnings to supplier factories 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. Figures for 2018 include warning letters which were still active and being enforced at adidas suppliers in 2018.

wages, social and medical insurance, hazardous chemicals management, overtime, deductions, transparency and safety controls in high-risk areas.

- **Terminations:** In 2018, we terminated agreements with one supplier for compliance reasons (2017: 4), as the supplier refused to grant the SEA team access to audit the factory. [SEE TABLE 50](#) 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.

### Number of business relationship terminations due to compliance problems

50

Region	2018	2017
Asia	1	4
Americas	0	0
EMEA	0	0
Global	1	4

# 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. 237](#) 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 Standard 'Core' option. The GRI content index can be found online. [ADIDAS-GROUP.COM/S/REPORTING-APPROACH](https://www.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. 103](#)

 [SEE MANAGEMENT ASSESSMENT OF PERFORMANCE, RISKS AND OPPORTUNITIES, AND OUTLOOK, P. 144](#)

## Consumer matters

— Consumer satisfaction

 [SEE INTERNAL MANAGEMENT SYSTEM, P. 103](#)

 [SEE MANAGEMENT ASSESSMENT OF PERFORMANCE, RISKS AND OPPORTUNITIES, AND OUTLOOK, P. 144](#)

## 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](#)

03

# GROUP MANAGEMENT MENT REPORT

FINANCIAL REVIEW

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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 51](#) Sales and operating profit growth, paired with a focus on management of operating working capital, are the main contributors to operating cash flow 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 51](#) 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. 41](#)

### 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.

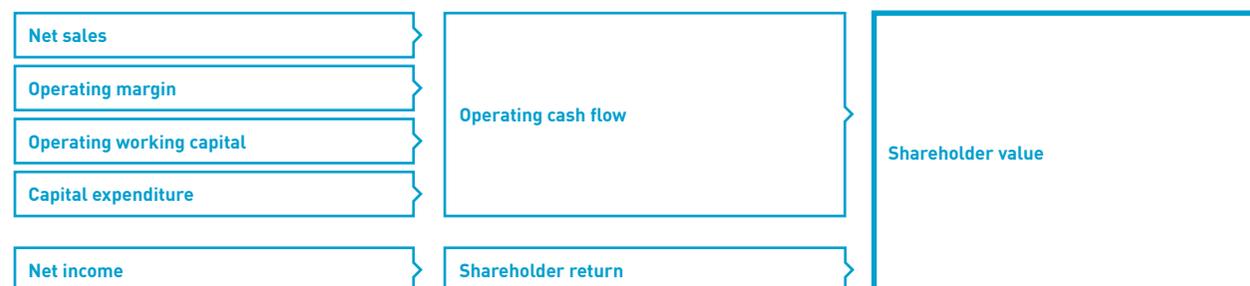
Therefore, we are committed to improving the efficiency of our marketing investments. This includes concentrating our communication efforts on key global brand initiatives and focusing our promotion spend on well-selected partnerships with top events, leagues, clubs, federations, athletes and artists. 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)

51



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 is another major lever to maximize our operating cash flow. We control capital expenditure with a top-down, bottom-up approach. 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.

### FOCUS ON NET INCOME IN THE INTEREST OF OUR SHAREHOLDERS

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 KPIs. [SEE DIAGRAM 51](#) Our strong focus on driving sustainable expansion to the company's bottom line is also reflected in the fact that, as part of the 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. 41](#)

### 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):**  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.

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.

**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 regarding in 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. 144](#) 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 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.

**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. In 2018, we continued to fine-tune our approach and system

platform for measuring the level of employee engagement that was implemented the year before. [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. 144](#) 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 this 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 regularly monitored and compared against initial targets as well as rolling forecasts on a monthly basis and latest estimates. 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 expected full year financial performance is assessed on a monthly basis. In this respect, also backlogs and sell-through data as well as 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 2018, adidas recorded strong operational and financial improvements. Revenues increased 8% on a currency-neutral basis, driven by high-single-digit growth at the adidas brand, slightly offset by a low-single-digit sales decrease at Reebok. With regard to major market segments, both North America and Asia-Pacific recorded double-digit currency-neutral sales increases, while Europe remained flat. The gross margin increased 1.4 percentage points to 51.8%, mainly reflecting positive effects from a better pricing, channel and product mix. Other operating expenses as a percentage of sales were up 0.5 percentage points to 41.9%, predominantly driven by higher marketing expenditure. The company's operating margin increased 1.1 percentage points to 10.8%, mainly reflecting the gross margin increase, which more than offset the investment-led increase in other operating expenses as a percentage of sales. Excluding the negative one-time tax impact recorded in 2017, net income from continuing operations increased 20% to € 1.709 billion. This translates into basic EPS from continuing operations of € 8.46, representing an increase of 20% versus the prior year period.

## ECONOMIC AND SECTOR DEVELOPMENT

### GLOBAL ECONOMIC GROWTH STEADY IN 2018<sup>1</sup>

The global economy kept its pace during 2018, with global gross domestic product (GDP) growing at 3.0%. However, international trade and investment have softened, not least due to increased trade protectionism and tariffs. Moreover,

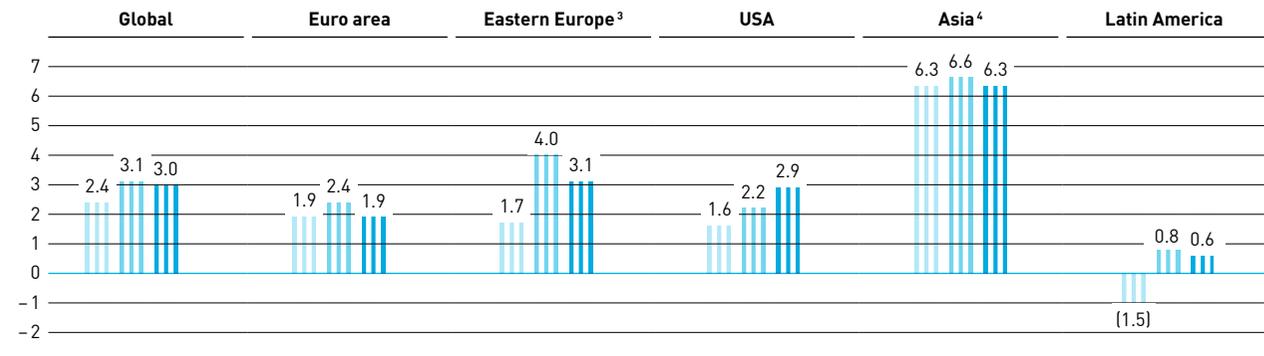
the ongoing withdrawal of monetary policy accommodation in developed economies has led to some tightening of global financing conditions. Developed economies grew 2.2% in 2018, supported by robust labor markets and some remaining fiscal stimuli. Nevertheless, topics around international relations such as trade disputes and the ongoing Brexit negotiations remained a political overhang and a drag on economic activity. Developing economies in aggregate grew 4.2%, even though macroeconomic conditions deteriorated in some countries, particularly in Latin America. Furthermore, the recovery among commodity exporters has lost momentum. Across the globe, risks of escalating geopolitical tensions, in particular around trade and tariffs, have increased.

### ROBUST GROWTH IN THE SPORTING GOODS INDUSTRY CONTINUES

The global sporting goods industry continued to grow at robust rates in 2018. North America returned to stronger industry growth rates after the slowdown in the two preceding years. Europe remained steady at a moderate pace, while China again outgrew the global industry. Most other markets also expanded, driven by continued 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 a predominant theme, as community workouts and related

Regional GDP development<sup>1,2</sup> in %

52



Legend: 2016 (light blue), 2017 (medium blue), 2018 (dark blue)

<sup>1</sup> Real change in percent versus prior year; 2016 and 2017 figures restated compared to prior year.

<sup>2</sup> Source: World Bank.

<sup>3</sup> Includes Emerging Europe and Central Asia.

<sup>4</sup> Includes East Asia and Pacific.

social media activities continue to be in favor. The e-commerce channel continued to see further expansion, as retailers are leveraging technologies both online and offline in order to be able to offer a seamless consumer journey. In addition, the 2018 FIFA World Cup provided a modest tailwind to the overall industry. From a category perspective, athletic footwear continued to be a strong growth driver for the industry in 2018, supported by ongoing high demand for various casual and running styles. Underlying demand for athletic apparel remained robust, as consumers continued to reallocate wallet share away from traditional apparel. The equipment category recorded another mixed year in 2018. For the sporting goods industry, too, risks related to trade protectionism and geopolitical tensions have increased.

Exchange rate development<sup>1</sup> € 1 equals

53

	Average rate 2017	Q1 2018	Q2 2018	Q3 2018	Q4 2018	Average rate 2018
USD	1.1266	1.2321	1.1658	1.1576	1.1450	1.1813
GBP	0.8754	0.8749	0.8861	0.8873	0.8945	0.8847
JPY	126.24	131.15	129.04	131.23	125.85	130.40
RUB	65.560	70.556	73.162	75.928	79.544	73.920
CNY	7.6116	7.7476	7.7136	7.9634	7.8584	7.8051

1 Spot rates at quarter-end.

## INCOME STATEMENT

IMPLEMENTING MORE GRANULAR VIEW OF  
OPERATING EXPENSES IN CONTEXT OF  
ADOPTION OF IFRS 9

In the context of the adoption of IFRS 9 and consequential amendments to IAS 1, adidas adjusted the presentation of other operating income and other operating expenses in order to allow for a more granular view of the company's operating expenses in the annual consolidated income statement. As of 2018, other operating expenses are derived from a functional logic and reported in the following line items: marketing and point-of-sale expenses, distribution and selling expense, general and administration expenses and sundry expenses. Furthermore, as required by the amendments to IAS 1, impairments of financial assets are presented as a separate line item within other operating expenses in the company's annual consolidated income statement. Prior year figures are adjusted accordingly.

■ SEE CONSOLIDATED INCOME STATEMENT, P. 150, ■ SEE NOTE 34, P. 212

ADIDAS DELIVERS STRONG FINANCIAL  
PERFORMANCE IN 2018

In 2018, revenues increased 8% on a currency-neutral basis. In euro terms, revenues grew 3% to € 21.915 billion from € 21.218 billion in 2017. ■ SEE DIAGRAM 54 From a market segment perspective, currency-neutral sales grew at double-digit rates in North America and Asia-Pacific while increasing at single-digit rates in Latin America and Russia/CIS. Currency-neutral sales remained stable in Europe and declined at a low-single-digit rate in Emerging Markets. ■ SEE BUSINESS PERFORMANCE BY SEGMENT, P. 125

Net sales  
+ 8%  
C.N.  
€ 21.915 bn

Net sales<sup>1,2</sup> € in millions

54

2018	21,915
2017	21,218
2016	18,483
2015	16,915
2014	14,534

1 2018, 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 and 2014 figures reflect continuing operations as a result of the divestiture of the Rockport business.

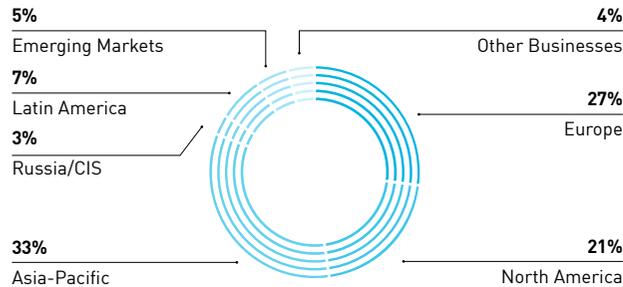
Net sales by segment<sup>1,2</sup> € in millions

55

	2018	2017	Change	Change (currency- neutral)
Europe	5,885	5,932	(1%)	0%
North America	4,689	4,275	10%	15%
Asia-Pacific	7,141	6,403	12%	15%
Russia/CIS	595	660	(10%)	1%
Latin America	1,634	1,907	(14%)	6%
Emerging Markets	1,144	1,300	(12%)	(3%)
Other Businesses	829	739	12%	15%
<b>Total</b>	<b>21,915</b>	<b>21,218</b>	<b>3%</b>	<b>8%</b>

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

2 Segmental structure adjusted compared to prior year, see Note 40.

Net sales by segment<sup>1,2</sup> in % of net sales 56

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

<sup>2</sup> Segmental structure adjusted compared to prior year, see Note 40.

## ADIDAS BRAND REVENUES GROW AT A HIGH-SINGLE-DIGIT RATE

Currency-neutral revenues for the adidas brand increased 9% with a double-digit sales increase in *Sport Inspired*

**adidas brand net sales** [SEE GLOSSARY](#) as well as a high-single-digit gain in *Sport Performance* [SEE GLOSSARY](#), the latter driven by double-digit sales growth in the training and running categories. In euro terms, adidas brand revenues grew 5% to € 19.851 billion compared to € 18.993 billion in 2017. Currency-neutral Reebok brand sales were down 3% versus the prior year, as double-digit sales growth in Classics was offset by a decline in Sport. In euro terms, Reebok sales decreased 8% to € 1.687 billion (2017: € 1.843 billion).

**+9% C.N.**  
€ 19.851 bn

**Reebok brand net sales**

**(-3%) C.N.**  
€ 1.687 bn

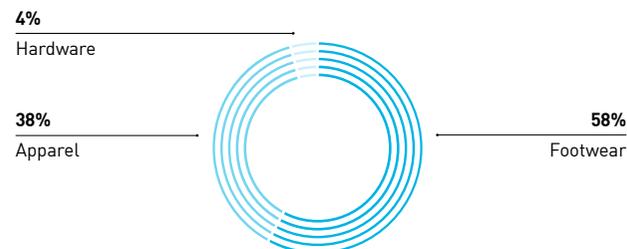
## SALES GROW IN FOOTWEAR AND APPAREL

Currency-neutral footwear sales grew 8% in 2018 due to double-digit growth in Sport Inspired and a high-single-digit gain in Sport Performance, the latter driven by double-digit sales increases in the training and running categories. Apparel revenues grew 11% on a currency-neutral basis due to double-digit increases in both Sport Inspired and Sport Performance, with the latter driven by double-digit gains in the training and football categories. Currency-neutral accessory and hardware sales were down 9%. [SEE DIAGRAM 57](#)

Net sales by product category<sup>1</sup> € in millions 57

	2018	2017	Change	Change (currency-neutral)
Footwear	12,783	12,427	3%	8%
Apparel	8,223	7,747	6%	11%
Hardware	910	1,044	(13%)	(9%)
<b>Total</b>	<b>21,915</b>	<b>21,218</b>	<b>3%</b>	<b>8%</b>

<sup>1</sup> 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 category<sup>1</sup> in % of net sales 58

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

## COST OF SALES REMAINS STABLE

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 2018, cost of sales was € 10.552 billion, remaining relatively stable compared to the prior year level of € 10.514 billion, as the growth of our business and less favorable exchange rates were offset by lower input costs due to efficiency gains.

## GROSS MARGIN IMPROVES 1.4 PERCENTAGE POINTS

In 2018, the gross profit increased 6% to € 11.363 billion from € 10.703 billion in 2017, representing a gross margin increase of 1.4 percentage points to 51.8% (2017: 50.4%). [SEE DIAGRAM 59](#)

This development was due to the positive effects from a better pricing, channel and product mix as well as lower input costs, which more than offset significant negative currency effects.

Gross margin<sup>1,2,3</sup> in % 59

2018	51.8
2017	50.4
2016	49.2
2015	48.3
2014	47.6

<sup>1</sup> Gross margin = [gross profit / net sales] × 100.

<sup>2</sup> 2018, 2017 and 2016 figures reflect continuing operations as a result of the divestiture of the Rockport, TaylorMade, Adams Golf, Ashworth and CCM Hockey businesses.

<sup>3</sup> 2015 and 2014 figures reflect continuing operations as a result of the divestiture of the Rockport business.

## ROYALTY AND COMMISSION INCOME INCREASES

Royalty and commission income increased 16% on a currency-neutral basis and 12% in euro terms to € 129 million (2017: € 115 million).

## OTHER OPERATING INCOME INCREASES

In 2018, other operating income increased 188% to € 48 million from € 17 million in 2017, mainly due to higher income from reimbursements of custom duties and sub-licensing of trademarks.

## OTHER OPERATING EXPENSES AS A PERCENTAGE OF SALES UP 0.5 PERCENTAGE POINTS

Other operating expenses, including depreciation and amortization, mainly consist of marketing and point-of-sale, distribution and selling as well as general and administration expenses. In 2018, other operating expenses were up 5% to € 9.172 billion (2017: € 8.766 billion), mainly reflecting increases in marketing investments. ■ [SEE NOTE 34, P. 212](#) As a percentage of sales, other operating expenses increased 0.5 percentage points to 41.9% from 41.3% in 2017. ■ [SEE DIAGRAM 60](#) Marketing and point-of-sale expenses amounted to € 3.001 billion in 2018 compared to € 2.724 billion in the prior year, representing an increase of 10% compared to the 2017 level. This increase mainly reflects activities related to the 2018 FIFA World Cup as well as overproportionate investments into our brands and the sell-through of our products. As a percentage of sales, marketing and point-of-sale expenses increased 0.9 percentage points to 13.7% (2017: 12.8%). ■ [SEE DIAGRAM 61](#) Distribution and selling expenses increased 3% to € 4.450 billion in 2018 from € 4.307 billion in the prior year, as investments into e-commerce and logistics infrastructure were partially offset by leveraging the distribution network. As a percentage of sales, distribution and selling expenses remained stable compared to the prior year. General and

### Other operating expenses<sup>1,2</sup> in % of net sales 60

2018		41.9
2017		41.3
2016		41.9
2015		42.6
2014		42.0

<sup>1</sup> 2018, 2017 and 2016 figures reflect continuing operations as a result of the divestiture of the Rockport, TaylorMade, Adams Golf, Ashworth and CCM Hockey businesses.

<sup>2</sup> 2015 and 2014 figures reflect continuing operations as a result of the divestiture of the Rockport business.

### Marketing and point-of-sale expenses<sup>1,2</sup> in % of net sales 61

2018		13.7
2017		12.8
2016		13.0
2015		13.9
2014		13.2

<sup>1</sup> 2018, 2017 and 2016 figures reflect continuing operations as a result of the divestiture of the Rockport, TaylorMade, Adams Golf, Ashworth and CCM Hockey businesses.

<sup>2</sup> 2015 and 2014 figures reflect continuing operations as a result of the divestiture of the Rockport business.

administration expenses remained stable at € 1.576 billion (2017: € 1.568 billion), as investments into digital systems and IT were compensated by overheads cost control. As a percentage of sales, general and administration expenses decreased 0.2 percentage points to 7.2% (2017: 7.4%).

## EBITDA INCREASES 15%

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 15% to € 2.882 billion in 2018 versus € 2.511 billion in 2017. ■ [SEE DIAGRAM 62](#) Depreciation and

amortization expense for tangible and intangible assets (excluding impairment losses/reversal of impairment losses) increased 8% to € 486 million in 2018 (2017: € 452 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 and trademarks) are tested annually and additionally when there are indications of potential impairment. In this connection, no impairment of intangible assets with unlimited useful lives incurred in 2018.

### EBITDA<sup>1,2,3</sup> € in millions 62

2018		2,882
2017		2,511
2016		1,953
2015		1,475
2014		1,283

<sup>1</sup> EBITDA = Income before taxes (IBT) + net interest expenses + depreciation and amortization.

<sup>2</sup> 2018, 2017 and 2016 figures reflect continuing operations as a result of the divestiture of the Rockport, TaylorMade, Adams Golf, Ashworth and CCM Hockey businesses.

<sup>3</sup> 2015 and 2014 figures reflect continuing operations as a result of the divestiture of the Rockport business.

## OPERATING MARGIN INCREASES 1.1 PERCENTAGE POINTS

Operating profit grew 14% to € 2.368 billion in 2018 versus € 2.070 billion in 2017. ■ [SEE DIAGRAM 63](#) This represents an operating margin increase of 1.1 percentage points to 10.8% compared to the prior year level of 9.8%. ■ [SEE DIAGRAM 64](#) This development was mainly due to the gross margin increase, which more than offset the investment-led increase in other operating expenses as a percentage of sales.

Operating margin  

 10.8 %

**NET FINANCIAL RESULT IMPROVES**

Financial income increased 24% to € 57 million in 2018 (2017: € 46 million), while financial expenses were down 50% to € 47 million compared to € 93 million in 2017. This development was due to lower impairment losses on other financial assets, lower interest expenses and positive exchange rate effects. As a result, the company recorded net financial income of € 10 million, compared to net financial expenses of € 47 million in 2017. [SEE DIAGRAM 65](#)

**Operating profit<sup>1,2,3,4</sup> € in millions** **63**

2018	2,368
2017	2,070
2016	1,582
2015	1,094
2014	961

<sup>1</sup> 2018, 2017 and 2016 figures reflect continuing operations as a result of the divestiture of the Rockport, TaylorMade, Adams Golf, Ashworth and CCM Hockey businesses.

<sup>2</sup> 2015 and 2014 figures reflect continuing operations as a result of the divestiture of the Rockport business.

<sup>3</sup> 2015 excluding goodwill impairment of € 34 million.

<sup>4</sup> 2014 excluding goodwill impairment of € 78 million.

**Operating margin<sup>1,2,3,4,5</sup> in %** **64**

2018	10.8
2017	9.8
2016	8.6
2015	6.5
2014	6.6

<sup>1</sup> Operating margin = (operating profit / net sales) × 100.

<sup>2</sup> 2018, 2017 and 2016 figures reflect continuing operations as a result of the divestiture of the Rockport, TaylorMade, Adams Golf, Ashworth and CCM Hockey businesses.

<sup>3</sup> 2015 and 2014 figures reflect continuing operations as a result of the divestiture of the Rockport business.

<sup>4</sup> 2015 excluding goodwill impairment of € 34 million.

<sup>5</sup> 2014 excluding goodwill impairment of € 78 million.

**Net financial result € in millions** **65**

2018	10
2017	(47)
2016	(46)
2015	(21)
2014	(48)

**TAX RATE DECREASES 1.2 PERCENTAGE POINTS TO 28.1%**

Excluding the negative one-time tax impact recorded in 2017, the company's tax rate decreased 1.2 percentage points to 28.1% in 2018 (2017: 29.3%).

Including the negative one-time tax impact in 2017, the company's tax rate decreased 4.9 percentage points to 28.1% (2017: 33.0%).

**NET INCOME FROM CONTINUING OPERATIONS UP 20% TO € 1.709 BILLION**

Excluding the negative one-time tax impact recorded in 2017, net income from continuing operations increased 20% to € 1.709 billion versus € 1.430 billion in the prior year. [SEE DIAGRAM 66](#) Basic EPS from continuing operations increased 20% to € 8.46 from € 7.05 in 2017. [SEE DIAGRAM 67](#) Diluted EPS from continuing operations was up 21% to € 8.45 in 2018 (2017: € 7.00).

Including the negative one-time tax impact in 2017, net income from continuing operations rose 26% to € 1.709 billion (2017: € 1.354 billion). Basic EPS from continuing operations increased 27% from € 6.68 in 2017 to € 8.46 in 2018. Diluted

EPS from continuing operations was up 27% to € 8.45 in 2018 compared to € 6.63 in 2017.

The total number of shares outstanding decreased by 4,689,889 shares in 2018 to 199,171,345. This was a result of shares repurchased as part of the company's share buyback program, which was partly offset by the last share conversions in relation to the company's 2012 convertible bond. [SEE FINANCIAL HIGHLIGHTS, P. 4](#) Consequently, the average number of shares used in the calculation of basic earnings per share (EPS) was 201,759,012 (2017: 202,391,673).

**Net income from continuing operations<sup>1,2,3</sup> € in millions** **66**

2018	1,709
2017	1,430
2016	1,082
2015	720
2014	642

<sup>1</sup> 2017 excluding negative one-time tax impact of € 76 million.

<sup>2</sup> 2015 excluding goodwill impairment of € 34 million.

<sup>3</sup> 2014 excluding goodwill impairment of € 78 million.

**Basic earnings per share<sup>1,2,3,4</sup> in €** **67**

2018	8.46
2017	7.05
2016	5.39
2015	3.54
2014	3.05

<sup>1</sup> Figures reflect continuing operations.

<sup>2</sup> 2017 excluding negative one-time tax impact of € 76 million.

<sup>3</sup> 2015 excluding goodwill impairment of € 34 million.

<sup>4</sup> 2014 excluding goodwill impairment of € 78 million.

## LOSSES FROM DISCONTINUED OPERATIONS AMOUNT TO € 5 MILLION

In 2018, adidas incurred losses from discontinued operations of € 5 million, net of tax, mainly related to the Rockport business (2017: losses of € 254 million).

## NET INCOME ATTRIBUTABLE TO SHAREHOLDERS INCREASES 45% TO € 1.702 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 45% to € 1.702 billion (2017: € 1.173 billion), excluding the negative one-time tax impact recorded in 2017. As a result, basic EPS from continuing and discontinued operations increased 46% to € 8.44 versus € 5.79 in 2017, while diluted EPS from continuing and discontinued operations grew 46% to € 8.42 (2017: € 5.75).

Including the negative one-time tax impact in 2017, the company's net income attributable to shareholders increased 55% to € 1.702 billion (2017: € 1.097 billion). Basic EPS from continuing and discontinued operations increased 56% to € 8.44 (2017: € 5.42) and diluted EPS from continuing and discontinued operations grew 57% to € 8.42 (2017: € 5.38).

## STATEMENT OF FINANCIAL POSITION AND STATEMENT OF CASH FLOWS

### ASSETS

At the end of December 2018, total assets were up 11% to € 15.612 billion versus € 14.019 billion in the prior year, as a result of an increase in both current assets as well as non-current assets. [SEE DIAGRAM 68](#)

Total current assets increased 14% to € 9.813 billion at the end of December 2018 compared to € 8.645 billion in 2017. Cash and cash equivalents were up 64% to € 2.629 billion at the end of December 2018 from € 1.598 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 € 29 million. Inventories decreased 7% to € 3.445 billion at the end of December 2018 from € 3.692 billion in 2017. [SEE NOTE 10, P. 173](#), [SEE DIAGRAM 70](#) On a currency-neutral basis, inventories decreased 5%, reflecting the company's focus on tight inventory management.

### Structure of statement of financial position<sup>1</sup> in % of total assets 68

	2018	2017 <sup>2</sup>
<b>Assets (€ in millions)</b>	<b>15,612</b>	14,019
Cash and cash equivalents	16.8	11.4
Accounts receivable	15.5	16.5
Inventories	22.1	26.3
Fixed assets <sup>3</sup>	30.7	31.5
Other assets	14.9	14.2

— 2018 — 2017

<sup>1</sup> For absolute figures see Consolidated Statement of Financial Position, p. 148.

<sup>2</sup> Restated according to IAS 8, see Note 03.

<sup>3</sup> Fixed assets = property, plant and equipment + goodwill + trademarks + other intangible assets + long-term financial assets.

Accounts receivable increased 4% to € 2.418 billion at the end of December 2018 (2017: € 2.315 billion). [SEE NOTE 08, P. 171](#), [SEE DIAGRAM 71](#) On a currency-neutral basis, receivables were up 5%, mainly reflecting the company's top-line development in 2018. Other current financial assets increased 38% to € 542 million at the end of December 2018 from € 393 million in 2017. [SEE NOTE 09, P. 172](#) This development was mainly due to an increase in the fair value of financial instruments. Other current assets were up 46% to € 725 million at the end of December 2018 (2017: € 498 million), mainly due to the change in the accounting treatment regarding IFRS 15, which led to the recognition of return assets. [SEE NOTE 11, P. 173](#)

Total non-current assets increased 8% to € 5.799 billion at the end of December 2018 from € 5.374 billion in 2017. Fixed assets increased 9% to € 4.798 billion at the end of December 2018 versus € 4.417 billion in 2017. Additions of € 854 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 and positive currency effects of € 58 million were partly offset by depreciation and amortization of € 494 million. Other

### Structure of statement of financial position<sup>1</sup> in % of total liabilities and equity 69

	2018	2017 <sup>2</sup>
<b>Liabilities and equity (€ in millions)</b>	<b>15,612</b>	14,019
Short-term borrowings	0.4	1.0
Accounts payable	14.7	14.1
Long-term borrowings	10.3	7.0
Other liabilities	33.8	35.0
Total equity	40.8	42.9

— 2018 — 2017

<sup>1</sup> For absolute figures see Consolidated Statement of Financial Position, p. 148.

<sup>2</sup> Restated according to IAS 8, see Note 03.

non-current financial assets increased 17% to € 256 million from € 219 million at the end of 2017. [SEE NOTE 17, P. 177](#) This development was mainly due to an increase in derivatives used to fully hedge the economic exposure related to the equity-neutral convertible bond. Deferred tax assets increased 3% to € 651 million from € 630 million in 2017.

#### Inventories € in millions 70

2018	3,445
2017	3,692
2016	3,763
2015	3,113
2014	2,526

#### Accounts receivable € in millions 71

2018	2,418
2017	2,315
2016	2,200
2015	2,049
2014	1,946

#### Accounts payable € in millions 72

2018	2,300
2017	1,975
2016	2,496
2015	2,024
2014	1,652

## LIABILITIES AND EQUITY

Total current liabilities increased 9% to € 6.834 billion at the end of December 2018 from € 6.291 billion in 2017. Short-term borrowings declined 51% to € 66 million at the end of December 2018 (2017: € 137 million), reflecting conversions of the company's convertible bond into adidas AG shares as well as a decrease in bank loans. Accounts payable were up 16% to € 2.300 billion at the end of December 2018 versus € 1.975 billion in 2017. [SEE DIAGRAM 72](#) On a currency-neutral basis, accounts payable increased 17%, reflecting the company's focus on efficient working capital management as well as improved terms with our suppliers. Other current financial liabilities were down 49% to € 186 million from € 362 million in 2017, mainly as a result of a decrease in the negative fair value of financial instruments. [SEE NOTE 20, P. 178](#) Other current provisions increased 66% to € 1.232 billion at the end of December 2018 versus € 741 million in 2017, mainly due to the change in the accounting treatment regarding IFRS 15, which led to an increase in the provision for returns. Current accrued liabilities grew 6% to € 2.305 billion at the end of December 2018 from € 2.180 billion in 2017, 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 1% to € 477 million at the end of December 2018 from € 473 million in 2017. [SEE NOTE 23, P. 180](#)

Total non-current liabilities increased 41% to € 2.414 billion at the end of December 2018 from € 1.711 billion in the prior year. Long-term borrowings were up 64% to € 1.609 billion at the end of December 2018 from € 983 million in the prior year, mainly driven by the issuance of the € 500 million equity-neutral convertible bond. [SEE NOTE 19, P. 177](#) Other non-current financial liabilities were up 358% to € 103 million at the end of December 2018 from € 22 million in the prior year. This was

mainly due to an increase in finance lease obligations related to two buildings at the company's headquarters in Herzogenaurach. Other non-current provisions increased 60% to € 128 million at the end of December 2018 from € 80 million in the prior year, mainly as a result of an increase in provisions for personnel. Non-current accrued liabilities decreased 78% to € 19 million from € 85 million in 2017 due to a decrease in accruals for personnel. [SEE NOTE 22, P. 179](#)

Shareholders' equity increased to € 6.377 billion at the end of December 2018 versus € 6.032 billion in 2017, driven by the net income generated during the year, an increase in hedging reserves of € 231 million and the reissuance of treasury shares in the amount of € 53 million. These developments were partly offset by the repurchase of treasury shares in the amount of € 1.021 billion, including incidental purchasing costs, and the dividend of € 528 million paid to shareholders for the 2017 financial year. The company's equity ratio decreased to 40.8% compared to 43.0% in the prior year, as the increase in shareholders' equity was more than offset by a balance sheet extension. [SEE NOTE 27, P. 184](#), [SEE DIAGRAM 73](#)

#### Equity ratio in % 73

2018	40.8
2017 <sup>1</sup>	43.0
2016	42.6
2015	42.5
2014	45.3

<sup>1</sup> Restated according to IAS 8, see Note 03.

## OPERATING WORKING CAPITAL

Operating working capital decreased 12% to € 3.563 billion at the end of December 2018 compared to € 4.033 billion in 2017. On a currency-neutral basis, operating working capital was down 10%. Average operating working capital as a percentage of sales from continuing operations decreased 1.4 percentage points to 19.0% [2017: 20.4%], reflecting the top-line development during the last twelve months as well as the company's continued focus on tight working capital management. [SEE DIAGRAM 74](#)

### Average operating working capital<sup>1,2,3</sup> in % of net sales **74**

Year	Average operating working capital in % of net sales
2018	19.0
2017	20.4
2016	21.1
2015	20.5
2014	22.4

<sup>1</sup> Average operating working capital = sum of operating working capital at quarter-end / 4.  
Operating working capital = accounts receivable + inventories – accounts payable.

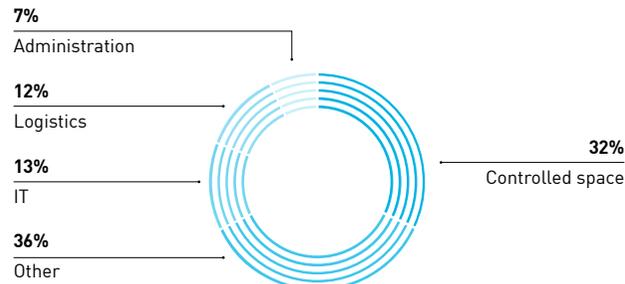
<sup>2</sup> 2018, 2017 and 2016 figures reflect continuing operations as a result of the divestiture of the Rockport, TaylorMade, Adams Golf, Ashworth and CCM Hockey businesses.

<sup>3</sup> 2015 and 2014 figures reflect continuing operations as a result of the divestiture of the Rockport business.

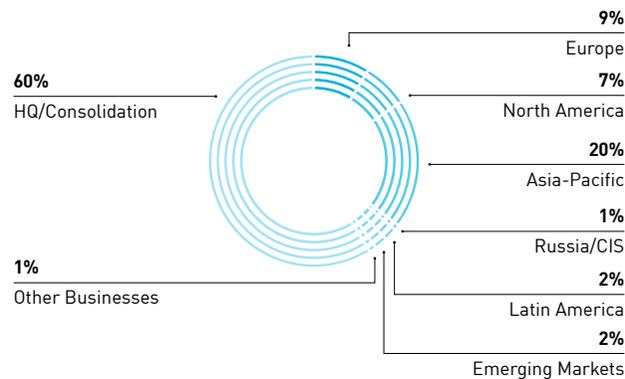
## INVESTMENT ANALYSIS

Capital expenditure is defined as the total cash expenditure for the purchase of tangible and intangible assets (excluding acquisitions). Capital expenditure increased 5% to € 794 million in 2018 (2017: € 755 million). Capital expenditure from continuing operations increased 6% to € 794 million from

### Capital expenditure by type in % of total CAPEX **75**



### Capital expenditure by segments in % of total CAPEX **76**



€ 752 million in 2017. Capital expenditure for property, plant and equipment was up 3% to € 699 million compared to € 681 million in the prior year. The company invested € 96 million in intangible assets, representing a 29% increase compared to the prior year (2017: € 74 million). Depreciation and amortization excluding impairment losses/reversal of impairment losses of tangible and intangible assets increased 12% to € 470 million in 2018 (2017: € 421 million).

Controlled space initiatives, which comprise 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 32% of total capital expenditure (2017: 48%). Expenditure for IT and logistics represented 13% and 12%, respectively (2017: 13% and 9%, respectively). In addition, expenditure for administration accounted for 7% (2017: 7%). Other initiatives, which mainly related to the expansion of the company's headquarters in Herzogenaurach, represented 36% of total capital expenditure (2017: 22%). [SEE DIAGRAM 75](#) From a segmental perspective, the majority of the capital expenditure was recorded at the company's headquarters in Herzogenaurach, Germany, accounting for 60% (2017: 47%). In addition, capital expenditure in Asia-Pacific accounted for 20% (2017: 21%) of the total capital expenditure, followed by Europe with 9% (2017: 10%), North America with 7% (2017: 8%), Latin America and Emerging Markets with 2% each (2017: 4% and 3%, respectively) as well as Russia/CIS with 1% (2017: 5%).

[SEE DIAGRAM 76](#)

## LIQUIDITY ANALYSIS

In 2018, net cash generated from operating activities increased to € 2.646 billion (2017: € 1.648 billion). [SEE FINANCIAL HIGHLIGHTS, P. 4](#) Net cash generated from continuing operating activities rose to € 2.666 billion (2017: € 1.641 billion), driven by

an increase in income before taxes and lower operating working capital requirements, partly offset by an increase in income taxes paid. Net cash used in investing activities decreased to € 636 million (2017: € 680 million). Net cash used in continuing investing activities also decreased to € 636 million (2017: € 676 million). The majority of continuing investing activities in 2018 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 further development of the company's headquarters in Herzogenaurach. Net cash used in financing activities and net cash used in continuing financing activities grew to € 951 million each (2017: € 769 million each), mainly due to the repurchase of treasury shares as well as the dividend paid to shareholders, partly offset by proceeds from the issue of a convertible bond and from long-term borrowings. Exchange rate effects negatively impacted the company's cash position by € 29 million. As a result of all these developments, cash and cash equivalents increased by € 1.031 billion to € 2.629 billion at the end of December 2018 compared to € 1.598 billion at the end of December 2017. [SEE DIAGRAM 78](#)

Net cash at December 31, 2018 amounted to € 959 million, compared to net cash of € 484 million in 2017, representing an improvement of € 475 million compared to the prior year. This development was driven by the increase in cash generated from operating activities, partly offset by the utilization of cash for the purchase of fixed assets as well as the repurchase of adidas AG shares and the dividend paid to shareholders. 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 -0.3 at the end of December 2018 (2017: -0.2), which is within the company's mid-term target corridor of below two times. [SEE DIAGRAM 77](#)

Operating cash flow, as described in the Internal Management System, increased 110% to € 2.529 billion in 2018 from € 1.202 billion in 2017, mainly due to the decrease in operating working capital. [SEE INTERNAL MANAGEMENT SYSTEM, P. 103](#)

#### Net borrowings/EBITDA<sup>1,2</sup> € in millions 77

2018		(0.3)
2017		(0.2)
2016		0.1
2015		0.3
2014		0.1

<sup>1</sup> 2018, 2017 and 2016 figures reflect continuing operations as a result of the divestiture of the Rockport, TaylorMade, Adams Golf, Ashworth and CCM Hockey businesses.

<sup>2</sup> 2015 and 2014 figures reflect continuing operations as a result of the divestiture of the Rockport business.

#### Change in cash and cash equivalents € in millions 78

Cash and cash equivalents at the end of 2017	Net cash generated from operating activities	Net cash used in investing activities	Net cash used in financing activities	Effect of exchange rates	Cash and cash equivalents at the end of 2018
1,598	2,646	(636)	(951)	(29)	2,629

#### 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 € 2.984 billion at December 31, 2018, compared to € 2.649 billion at the end of December 2017, representing an increase of 13%. [SEE NOTE 30, P. 192](#) At the end of December 2018, financial commitments for promotion and advertising increased 11% to € 5.828 billion in 2018 (2017: € 5.255 billion).

[SEE NOTE 42, P. 221](#)

## 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 NOTE 02, P. 158](#) 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, borrowings would become due and payable immediately. As at December 31, 2018, 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 nine years. In addition, we have an unused multi-currency commercial paper program in the amount of € 2.0 billion available (2017: € 2.0 billion). At the end of 2018, committed and uncommitted bilateral credit lines amounted to € 2.215 billion (2017: € 2.251 billion), of which € 2.008 billion was unutilized (2017: € 2.145 billion). Committed and uncommitted credit lines represent approximately 45% and 55% of total short-term bilateral credit lines, respectively (2017: 47% and 53%, respectively). [SEE DIAGRAM 81](#) 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** 79

	2018	2017
Bilateral credit lines	2,215	2,251
Eurobonds	984	983
Convertible bond	-	31
Equity-neutral convertible bond	484	-
<b>Total</b>	<b>3,683</b>	<b>3,265</b>

**Remaining time to maturity of available facilities € in millions** 80

	2018	2017
< 1 year	1,475	1,601
1 to 3 years	980	381
3 to 5 years	771	746
> 5 years	457	537
<b>Total</b>	<b>3,683</b>	<b>3,265</b>

**Bilateral credit lines € in millions** 81

	2018	2017
Committed	987	1,055
Uncommitted	1,228	1,196
<b>Total</b>	<b>2,215</b>	<b>2,251</b>

**OUTSTANDING BONDS**

The company has two outstanding eurobonds, both issued in 2014, and one outstanding equity-neutral convertible bond, which was issued in 2018. A convertible bond issued in 2012 was fully converted during 2018. 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%. The equity-neutral convertible bond of € 500 million was issued on September 5, 2018, with a coupon of 0.05% and is due on September 12, 2023. [SEE OUR SHARE, P. 57](#), [SEE NOTE 19, P. 177](#), [SEE TABLE 82](#)

**Issued bonds at a glance € in millions** 82

	Volume	Coupon	Maturity
Eurobond	€ 600	fixed	2021
Eurobond	€ 400	fixed	2026
Equity-neutral convertible bond	€ 500	fixed	2023

**GROSS BORROWINGS INCREASE**

The company's gross borrowings, the vast majority of which are denominated in euro, are composed of bank borrowings as well as the outstanding eurobonds and the equity-neutral convertible bond. Gross borrowings increased 50% to € 1.676 billion at the end of 2018 from € 1.120 billion in the prior year. This development was mainly due to the issuance of the € 500 million equity-neutral convertible bond. Including the company's eurobonds, the total amount of bonds outstanding at the end of 2018 was € 1.469 billion (2017: € 1.014 billion). Bank borrowings amounted to € 207 million compared to € 106 million in the prior year. [SEE TABLE 83](#)

**Financing structure € in millions** 83

	2018	2017
<b>Cash and short-term financial assets</b>	<b>2,635</b>	<b>1,604</b>
Bank borrowings	207	106
Eurobonds	984	983
Convertible bond	-	31
Equity-neutral convertible bond	484	-
<b>Gross total borrowings</b>	<b>1,676</b>	<b>1,120</b>
<b>Net cash</b>	<b>959</b>	<b>484</b>

**STABLE DEBT MATURITY PROFILE**

Over the course of 2018, the company's financing maturity profile remained stable. In 2019, assuming unchanged maturities, debt instruments of € 66 million will mature. This compares to € 137 million which matured during the course of 2018. [SEE DIAGRAM 84](#)

**Remaining time to maturity of gross borrowings € in millions** 84

	2018	2017
< 1 year	66	137
1 to 3 years	635	-
3 to 5 years	522	596
> 5 years	453	387
<b>Total</b>	<b>1,676</b>	<b>1,120</b>

■ 2018 ■ 2017

**NET CASH POSITION OF € 959 MILLION**

Net cash at December 31, 2018 amounted to € 959 million, compared to net cash of € 484 million in 2017, representing an improvement of € 475 million versus the prior year.

[SEE DIAGRAM 85](#) This development was driven by the increase in cash generated from operating activities, 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.

**Net cash/(net borrowings)<sup>1</sup> € in millions** 85

2018	959
2017	484
2016	(103)
2015	(460)
2014	(185)

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

**INTEREST RATE DECREASES**

The weighted average interest rate on the company's gross borrowings decreased to 2.1% in 2018 (2017: 2.7%). [SEE DIAGRAM 86](#) This development was mainly due to conversions of the convertible bond into adidas AG shares and a reduction of short-term borrowings. Fixed-rate financing represented 97% of total gross borrowings at the end of 2018 (2017: 91%). Variable-rate financing accounted for 3% of total gross borrowings at the end of the year (2017: 9%).

**Interest rate development<sup>1</sup> in %** 86

2018	2.1
2017	2.7
2016	2.3
2015	2.4
2014	3.1

<sup>1</sup> 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 2018, our Treasury department managed a net deficit of around US \$ 6.0 billion related to operational activities (2017: US \$ 6.6 billion). Thereof, around US \$ 3.8 billion was against the euro (2017: US \$ 3.8 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 2019 as of year-end 2018. At the same time, we have already started hedging our exposure for 2020. The use or combination of different hedging instruments, such as forward exchange contracts, currency options and swaps, protects us against unfavorable currency movements. [SEE NOTE 31, P. 194](#)

## 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 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, 46% of total assets as at December 31, 2018 related to financial assets (2017: 49%), which primarily consist of shares in affiliated companies. Intercompany accounts, through which transactions between affiliated companies are settled, represent another 26% of total assets (2017: 35%) and 45% of total liabilities and equity as at December 31, 2018 compared to 48% in the prior year.

### 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, 2018, 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 **87**

	2018	2017
Net sales	4,128	3,732
<b>Total output</b>	<b>4,128</b>	<b>3,732</b>
Other operating income	516	503
Cost of materials	(1,538)	(1,292)
Personnel expenses	(731)	(692)
Depreciation and amortization	(98)	(91)
Other operating expenses	(2,282)	(2,170)
<b>Operating profit</b>	<b>(5)</b>	<b>(10)</b>
Financial result	1,542	655
Taxes	(113)	(96)
<b>Net income</b>	<b>1,424</b>	<b>549</b>
Retained earnings brought forward	45	24
Allocation to other revenue reserves	(400)	0
Allocation to capital reserves	(9)	0
Utilization for the repurchase of treasury shares	(355)	0
<b>Retained earnings</b>	<b>705</b>	<b>573</b>

adidas AG net sales € in millions **88**

	2018	2017
Royalty and commission income	1,900	1,809
adidas Germany	1,157	1,027
Foreign subsidiaries	60	64
Central distribution	319	209
Other revenues	692	623
<b>Total</b>	<b>4,128</b>	<b>3,732</b>

### NET SALES INCREASE 11%

Sales of adidas AG comprise external revenues generated by adidas Germany with products of the adidas and Reebok brands as well as revenues from foreign subsidiaries. Revenues of adidas AG also include royalty and commission income, mainly from affiliated companies, revenues from central distribution, and other revenues. In 2018, adidas AG net sales grew 11% to € 4.128 billion compared to € 3.732 billion in the prior year. This growth was mainly due to higher sales at adidas Germany and an increase in revenues from central distribution. ■ [SEE TABLE 88](#)

### OTHER OPERATING INCOME UP 3%

In 2018, other operating income of adidas AG increased 3% to € 516 million (2017: € 503 million). This development was primarily due to positive currency effects.

### OTHER OPERATING EXPENSES INCREASE 5%

In 2018, other operating expenses for adidas AG rose 5% to € 2.282 billion (2017: € 2.170 billion). ■ [SEE TABLE 87](#) This was largely attributable to an increase in expenses for advertising and promotion, higher maintenance costs and higher other expenses, partly offset by a decrease in allowances for doubtful accounts.

**DEPRECIATION AND AMORTIZATION UP 8%**

Depreciation and amortization for adidas AG rose 8% to € 98 million in 2018 (2017: € 91 million), mainly as a result of an increase in depreciation and amortization of software.

**OPERATING RESULT INCREASES**

In 2018, adidas AG generated an operating loss of € 5 million, (2017: operating loss of € 10 million). [SEE TABLE 87](#) This development was primarily due to an increase in cost of materials as well as in other operating expenses and personnel expenses, which offset higher sales.

**FINANCIAL RESULT IMPROVES**

The financial result of adidas AG improved 135% to € 1.542 billion in 2018 (2017: € 655 million). The increase was attributable to higher income from dividends and higher profit transfers from affiliated companies under profit and loss transfer agreements.

**NET INCOME INCREASES SIGNIFICANTLY**

Net income, after taxes of € 113 million (2017: € 96 million), amounted to € 1.424 billion in 2018 and was thus 159% above the prior year level (2017: € 549 million). [SEE TABLE 87](#)

**BALANCE SHEET**

Balance sheet in accordance with HGB 89  
(Condensed) € in millions

	Dec. 31, 2018	Dec. 31, 2017
<b>Assets</b>		
Intangible assets	162	124
Property, plant and equipment	688	610
Financial assets	4,361	4,308
<b>Fixed assets</b>	<b>5,211</b>	<b>5,042</b>
Inventories	47	49
Receivables and other assets	2,655	3,262
Cash and cash equivalents, securities	1,478	337
<b>Current assets</b>	<b>4,180</b>	<b>3,648</b>
Prepaid expenses	100	168
Active difference from asset allocation	5	5
<b>Total assets</b>	<b>9,496</b>	<b>8,863</b>
<b>Equity and liabilities</b>		
Shareholders' equity	2,634	2,704
Provisions	699	624
Liabilities and other items	6,163	5,535
<b>Total equity and liabilities</b>	<b>9,496</b>	<b>8,863</b>

**TOTAL ASSETS ABOVE PRIOR YEAR**

At the end of December 2018, total assets grew 7% to € 9.496 billion compared to € 8.863 billion in the prior year. This development was mainly a result of increases in cash and cash equivalents, securities and fixed assets, partly offset by the decline in receivables and other assets. [SEE TABLE 89](#)

**SHAREHOLDERS' EQUITY DOWN 3%**

Shareholders' equity declined 3% to € 2.634 billion at the end of 2018 (2017: € 2.704 billion). [SEE TABLE 89](#) The equity ratio decreased to 27.7% (2017: 30.5%).

**PROVISIONS INCREASE 12%**

Provisions were up 12% to € 699 million at the end of 2018 (2017: € 624 million). [SEE TABLE 89](#) The increase primarily resulted from contingent losses from pending transactions as well as higher marketing provisions.

**LIABILITIES AND OTHER ITEMS UP 11%**

At the end of December 2018, liabilities and other items increased 11% to € 6.163 billion (2017: € 5.535 billion). [SEE TABLE 89](#) This development was mainly a result of the increase in liabilities related to the convertible bond and higher liabilities due to banks, partly offset by the decline in payables to affiliated companies.

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

adidas AG generated a positive cash flow from operating activities of € 1.696 billion (2017: € 1.109 billion). The change versus the prior year was mainly a result of the increase in net income as well as the increase in securities classified as current assets, partly offset by a decrease in payables to affiliated companies. Net cash outflow from investment activities was € 270 million (2017: € 330 million). This was primarily attributable to capital expenditure for tangible fixed assets in an amount of € 215 million and capital expenditure for financial assets in an amount of € 53 million. Financing activities resulted in a net cash outflow of € 889 million (2017: € 469 million). The net cash outflow from financing activities mainly relates to the dividend payment in an amount of € 528 million. As a result of all these developments, cash and cash equivalents of adidas AG increased to € 874 million at the end of December 2018 compared to € 337 million at the end of the prior year.

adidas AG has bilateral credit lines of € 1.4 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 AND EXPLANATORY REPORT

### COMPOSITION OF SUBSCRIBED CAPITAL

The nominal capital of adidas AG amounts to € 200,416,186 (as at December 31, 2018) 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'). In the 2018 financial year, the nominal capital and the number of shares were reduced due to the cancellation of 8,800,000 treasury shares and the capital reduction with effect from October 22, 2018. The shares are fully paid in. Any claim on the part of the shareholders to the issuance of individual share certificates is generally excluded pursuant to § 4 section 10 of the Articles of Association unless such issuance is required in accordance with the regulations applicable at a stock exchange where the shares are admitted. Pursuant to § 67 section 2 German Stock Corporation Act (Aktiengesetz – AktG), in relation to adidas AG, only a person who is registered as such in the share register shall be deemed a shareholder. Each share grants one vote at the Annual General Meeting and determines the shareholders' share in the company's profit. All shares carry the same rights and obligations. The shareholders' individual rights and obligations follow from the provisions of the AktG, in particular from §§ 12, 53a et seq., 118 et seq. and 186 AktG. As at December 31, 2018, adidas AG held 1,244,841 treasury shares, which do not confer any rights to the company in accordance with § 71b AktG. [SEE NOTE 27, P. 184](#)

In the USA, adidas AG has 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 adidas AG 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 and internal guidelines of adidas AG and based on Article 19 section 11 of the Regulation (EU) No 596/2014 (Market Abuse Regulation), however, particular trade prohibitions do exist for Executive Board members with regard to the purchase and sale of adidas AG shares, particularly in connection with the (time of) publication of interim financial reports or year-end reports.

In addition, restrictions of voting rights may exist pursuant to, inter alia, § 136 AktG or for treasury shares pursuant to § 71b AktG as well as due to capital market regulations, in particular pursuant to §§ 33 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 ceases.

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## 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 reaching or 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 enable 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 and 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. 21](#)

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 the Chairman of the Supervisory Board has two votes.

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

## AMENDMENTS TO THE ARTICLES OF ASSOCIATION

Pursuant to §§ 119 section 1 number 5, 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. 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). The Executive Board may, subject to Supervisory Board approval, exclude shareholders' subscription rights. The overall volume of the shares issued based on this authorization with the exclusion of subscription rights – together with shares issued against contributions in cash with a simplified exclusion of subscription rights from the Authorized Capital 2017/III – must not exceed 10% of the nominal capital existing at the date of the respective issuance. This deduction clause shall not apply if residual amounts of shares are excluded from subscription rights.

- 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). Any repurchased treasury shares of the company which are used by the company for employee stock purchase plans during the term of this authorization shall be attributed to the maximum number of 4,000,000 shares. Shareholders' subscription rights are excluded. The new shares may only be issued to (current or former) employees of the company and its affiliated companies as well as to (current and former) members of management bodies of the company's affiliated companies ('eligible persons').
- 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). The Executive Board may, subject to Supervisory Board approval, exclude residual amounts from shareholders' subscription rights.
- 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). The Executive Board may, subject to Supervisory Board approval, exclude residual amounts from shareholders' subscription rights. Additionally, the Executive Board may, subject to Supervisory Board approval, exclude shareholders' subscription rights when issuing the new shares at a value not significantly below the stock exchange value of the company's shares already quoted on the stock exchange at the point in time when the issue price is ultimately determined, which should be as close as possible to the placement of the shares; this exclusion of subscription rights may also be associated with the listing of the company's shares on a foreign stock

exchange. The authorization to exclude subscription rights pursuant to the previous sentence, however, may only be used to the extent that the pro rata amount of the new shares in the nominal capital together with the pro rata amount in the nominal capital of other shares which have been issued by the company since May 11, 2017, subject to the exclusion of subscription rights pursuant to or in accordance with § 186 section 3 sentence 4 AktG on the basis of an authorized capital or following a repurchase or for which subscription or conversion rights or subscription or conversion obligations have been granted since May 11, 2017, through the issuance of convertible bonds and/or bonds with warrants, with subscription rights excluded pursuant to § 186 section 3 sentence 4 AktG, does not exceed 10% of the nominal capital existing on the date of the entry of this authorization with the commercial register or – if this amount is lower – at the respective date on which the resolution on utilization of the authorization is adopted. The overall volume of the shares issued based on this authorization with the exclusion of subscription rights – together with shares issued from the Authorized Capital 2017/II – must not exceed 10% of the nominal capital existing at the date of the respective issuance. This deduction clause shall not apply if residual amounts of shares are excluded from subscription rights.

The above-mentioned authorizations are, in principle, cumulative authorizations. [SEE NOTE 27, P. 184](#)

### 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. In the 2018 financial year, the company exercised its right to redeem outstanding bonds early. The convertible bond was thus fully converted or redeemed and no more shares can be issued from the Contingent Capital 2010. The total number of shares issued to the bondholders amounted to a total of 6,139,227 shares.

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 2018). 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 9, 2018 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 9, 2018, the Executive Board is authorized to issue bonds with warrants and/or convertible bonds in an aggregate nominal value of up to € 2,500,000,000 with or without a limited term against contributions in cash once or several times until May 8, 2023, 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

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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. Treasury shares which are or will be sold in accordance with § 71 section 1 number 8 in conjunction with § 186 section 3 sentence 4 AktG between the starting date of the term of this authorization and the issuance of the respective bonds are attributed to the above-mentioned limit of 10%. Shares which are or will be issued, subject to the exclusion of subscription rights, in accordance with § 186 section 3 sentence 4 AktG or § 203 section 1 in conjunction with § 186 section 3 sentence 4 AktG between the starting date of the term of this authorization and the issuance of the respective bonds in the context of a cash capital increase are also attributed to the above-mentioned limit of 10%. Finally, shares for which there are option or conversion rights or obligations or a right to delivery of shares of the company in favor of the company due to bonds with warrants or convertible bonds issued by the company or its subordinated Group companies, subject to the exclusion of subscription rights, in accordance with § 221 section 4 sentence 2 in conjunction with § 186 section 3 sentence 4 AktG during the term of this authorization based on other authorizations are attributed to the above-mentioned limit of 10%. Notwithstanding the Supervisory Board's right to determine further approval requirements, the Executive Board requires the Supervisory Board's approval for the issuance of bonds with warrants and/or convertible bonds based on this authorization of the Annual General Meeting on May 9, 2018 with the exclusion of shareholders' subscription rights.

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 9, 2018.

### **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. The authorization furthermore sets out the lowest and highest nominal value that may be granted in each case.

The purposes for which treasury 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 on the stock exchange or through a public offer to all shareholders in relation to their shareholding quota; in case of an offer to all shareholders, subscription rights for residual amounts are excluded. The shares may also be sold differently, provided the shares are sold in exchange for a cash payment and at a price that, at the time of the sale, is not significantly below the stock market price of the company's shares with the same features; the prorated amount of the nominal capital which is attributable to the aggregate number of shares sold under this authorization may not exceed 10% of the nominal capital. The prorated amount of the nominal capital attributable to the new shares issued between May 12, 2016 and the sale of the shares based on an authorized capital with the exclusion of shareholders' subscription rights pursuant to § 203 section 1 in conjunction with § 186 section 3 sentence 4 AktG is taken into account in the limit of 10%. Likewise, the prorated amount of the nominal capital that is attributable to shares which may be issued due to bonds with warrants and/or convertible bonds which are linked to subscription or conversion rights or obligations or the company's right to delivery of shares, provided these bonds are issued on the basis of authorizations pursuant to §§ 221 section 4, 186 section 3 sentence 4 AktG between May 12, 2016 and the sale of the shares, shall also be attributed to the limit of 10%.
- 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

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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 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. The number of shares the company issues to eligible persons by partially utilizing the Authorized Capital 2016 must be attributed to the maximum number of 4,000,000 shares.
- They may be canceled without such cancellation requiring an additional resolution of the Annual General Meeting.

Furthermore, the shares may be promised or 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 cancellation of shares, shareholders' subscription rights are excluded.

The Supervisory Board may determine 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 2016 and 2017 financial years, the Executive Board partly utilized the authorization to repurchase adidas AG shares in the context of the share buyback program 2014 – 2017. In the year under review, the Executive Board resolved, following the approval of the Supervisory Board, to initiate another multi-year share buyback program and thus once again utilized the authorization to repurchase adidas AG shares. In a first tranche (total period from March 22, 2018 up to and including December 4, 2018) of this share buyback program, adidas AG bought back 5,089,879 adidas AG shares via the stock exchange in the year under review. ■ [SEE NOTE 27, P. 184](#)

- In the scope of the authorization resolved upon 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 the shares delivered for these equity derivatives were purchased in compliance with the principle of equal treatment. 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 cancellation 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 the material 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: Europe (formerly called Western Europe), North America adidas, North America Reebok, Asia-Pacific, Russia/CIS, Latin America, Emerging Markets (formerly called Middle East), adidas Golf, Runtastic and Other centrally managed businesses. The four former operating segments Greater China, Japan, South Korea and Southeast Asia/Pacific were consolidated to one operating segment Asia-Pacific effective January 1, 2018. While the operating segments Europe, Asia-Pacific, Russia/CIS, Latin America and Emerging Markets are reported separately, North America adidas and North America Reebok are combined to the reportable segment North America. Each reportable segment comprises all wholesale, retail and e-commerce business activities relating to the distribution and sale of products of the adidas and Reebok brands to retail customers and end consumers. The remaining operating segments are aggregated under Other Businesses due to their only subordinate materiality.

### EUROPE

In 2018, sales in Europe remained stable on a currency-neutral basis. In euro terms, sales in Europe declined 1% to **Net sales in Europe** € 5.885 billion from € 5.932 billion in 2017. adidas brand revenues remained stable on a currency-neutral basis, as growth in Sport Inspired was offset by a low-single-digit decrease in Sport Performance. Reebok brand revenues in Europe decreased 3% on a currency-neutral basis, as mid-single-digit sales growth in Classics was offset by a double-digit decline in Sport. ■ [SEE TABLE 90](#)

**0%**  
C.N.  
€ 5.885 bn

### Europe at a glance € in millions

90

	2018	2017	Change	Change (currency- neutral)
Net sales	5,885	5,932	(1%)	0%
adidas brand	5,405	5,434	(1%)	0%
Reebok brand	480	499	(4%)	(3%)
Gross margin	47.7%	45.7%	2.0pp	–
Segmental operating profit	1,176	1,192	(1%)	–
Segmental operating margin	20.0%	20.1%	(0.1pp)	–

Gross margin in Europe increased 2.0 percentage points to 47.7% from 45.7% in 2017 as positive effects from a more favorable pricing, product and channel mix as well as lower input costs more than offset the significant negative impact from unfavorable currency developments. Operating expenses were up 7% to € 1.628 billion versus € 1.519 billion in 2017. This development reflects an increase in marketing expenditure as well as higher operating overhead costs. Operating expenses as a percentage of sales were up 2.1 percentage points to 27.7% (2017: 25.6%). The operating margin decreased 0.1 percentage points to 20.0% (2017: 20.1%), as the gross margin improvement was offset by the negative effect of higher operating expenses as a percentage of sales. Operating profit in Europe decreased 1% to € 1.176 billion versus € 1.192 billion in the prior year. ■ [SEE TABLE 90](#)

### NORTH AMERICA

Revenues in North America grew 15% on a currency-neutral basis and 10% in euro terms to € 4.689 billion from **Net sales in North America** € 4.275 billion in 2017. adidas brand sales increased 17% on a currency-neutral basis with double-digit sales growth in both Sport Inspired and Sport Performance, the latter driven by double-digit sales growth in the running, training and football categories. Revenues of the Reebok brand in North America remained stable on a currency-neutral basis, as double-digit sales growth in Classics was offset by a double-digit decline in Sport. ■ [SEE TABLE 91](#)

**+15%**  
C.N.  
€ 4.689 bn

### North America at a glance € in millions

91

	2018	2017	Change	Change (currency- neutral)
Net sales	4,689	4,275	10%	15%
adidas brand	4,277	3,843	11%	17%
Reebok brand	411	432	(5%)	0%
Gross margin	41.2%	39.5%	1.7pp	–
Segmental operating profit	698	468	49%	–
Segmental operating margin	14.9%	10.9%	3.9pp	–

Gross margin in North America increased 1.7 percentage points to 41.2% (2017: 39.5%), driven by an improved pricing, product and channel mix, as well as lower input costs. Operating expenses were up 2% to € 1.305 billion versus € 1.280 billion in 2017, mainly reflecting an increase in marketing expenditure. Operating expenses as a percentage of sales decreased 2.1 percentage points to 27.8% (2017: 29.9%). As a result of the gross margin increase as well as the

positive effect of lower operating expenses as a percentage of sales, the operating margin improved 3.9 percentage points to 14.9% from 10.9% in 2017. Operating profit in North America increased 49% to € 698 million from € 468 million in 2017.

■ SEE TABLE 91

## ASIA-PACIFIC

Sales in Asia-Pacific grew 15% on a currency-neutral basis. In euro terms, sales in Asia-Pacific were up 12% to € 7.141 billion from € 6.403 billion in 2017. Revenues of brand adidas increased 16% on a currency-neutral basis. This development was due to double-digit sales growth in both Sport Inspired and Sport Performance, with the latter driven by double-digit gains in the training and running categories. Reebok brand sales in Asia-Pacific grew 3% on a currency-neutral basis, driven by high-single-digit sales increases in Classics, partly offset by a low-single-digit sales decline in Sport. ■ SEE TABLE 92

### Asia-Pacific at a glance € in millions

92

	2018	2017	Change	Change (currency- neutral)
Net sales	7,141	6,403	12%	15%
adidas brand	6,805	6,067	12%	16%
Reebok brand	336	337	0%	3%
Gross margin	56.2%	55.7%	0.5pp	-
Segmental operating profit	2,339	2,115	11%	-
Segmental operating margin	32.7%	33.0%	(0.3pp)	-

Gross margin in Asia-Pacific increased 0.5 percentage points to 56.2% (2017: 55.7%), as a more favorable pricing, product, and channel mix and lower input costs more than offset the negative impact from unfavorable currency developments. Operating expenses were up 15% to € 1.688 billion versus € 1.466 billion in 2017. This development reflects an increase in both marketing expenditure as well as operating overhead costs. Operating expenses as a percentage of sales were up 0.7 percentage points to 23.6% (2017: 22.9%). As a result of higher operating expenses as a percentage of sales, which more than offset the increase in gross margin, the operating margin was down 0.3 percentage points to 32.7% versus 33.0% in 2017. Operating profit in Asia-Pacific increased 11% to € 2.339 billion from € 2.115 billion in 2017. ■ SEE TABLE 92

## RUSSIA/CIS

Sales in Russia/CIS increased 1% on a currency-neutral basis, despite a significant amount of store closures in 2018.

### Net sales in Russia/CIS

+1%  
C.N.  
€ 595 m

In euro terms, sales in Russia/CIS declined 10% to € 595 million from € 660 million in 2017. adidas brand revenues were up 5% on a currency-neutral basis, as Sport Performance grew at a mid-single-digit rate while Sport Inspired remained stable. The former was due to exceptional growth in the football category, reflecting revenues generated through leveraging the 2018 FIFA World Cup. Revenues of the Reebok brand in Russia/CIS decreased 8% on a currency-neutral basis, driven by declines in Sport and, to a lesser extent, Classics. ■ SEE TABLE 93

### Russia/CIS at a glance € in millions

93

	2018	2017	Change	Change (currency- neutral)
Net sales	595	660	(10%)	1%
adidas brand	446	478	(7%)	5%
Reebok brand	149	182	(18%)	(8%)
Gross margin	65.8%	64.9%	0.9pp	-
Segmental operating profit	146	136	7%	-
Segmental operating margin	24.6%	20.6%	4.0pp	-

Gross margin in Russia/CIS increased 0.9 percentage points to 65.8% from 64.9% in 2017, despite a less favorable pricing and channel mix as well as significant negative currency effects. Operating expenses were down 16% to € 245 million (2017: € 292 million), mainly reflecting a decline in operating overhead costs. Operating expenses as a percentage of sales decreased 3.0 percentage points to 41.2% versus 44.3% in the prior year. As a result of the gross margin increase and the positive effect of lower operating expenses as a percentage of sales, the operating margin improved 4.0 percentage points to 24.6% from 20.6% in 2017. Operating profit in Russia/CIS increased 7% to € 146 million versus € 136 million in 2017.

■ SEE TABLE 93

**LATIN AMERICA**

Revenues in Latin America increased 6% on a currency-neutral basis. In euro terms, sales in Latin America **Net sales in Latin America** declined 14% to € 1.634 billion from € 1.907 billion in 2017. The first-time application of hyperinflation accounting according to IAS 29 in Argentina negatively impacted reported sales of the Latin America segment, whereas the impact on currency-neutral sales growth was slightly positive. Revenues of brand adidas were up 8% on a currency-neutral basis. This development was driven by a mid-single-digit sales increase at Sport Inspired while Sport Performance remained stable, despite a double-digit increase in the football category. Reebok brand sales in Latin America declined 12% on a currency-neutral basis, driven by a double-digit decline in Sport and a mid-single-digit decline in Classics. [SEE TABLE 94](#)

**Latin America at a glance** € in millions

94

	2018	2017	Change	Change (currency-neutral)
Net sales	1,634	1,907	(14%)	6%
adidas brand	1,463	1,673	(13%)	8%
Reebok brand	171	235	(27%)	(12%)
Gross margin	44.9%	42.1%	2.8pp	–
Segmental operating profit	279	268	4%	–
Segmental operating margin	17.1%	14.0%	3.0pp	–

+6%  
C.N.  
€ 1.634 bn

Gross margin in Latin America increased 2.8 percentage points to 44.9% (2017: 42.1%), as the very positive effect from a more favorable pricing mix and lower input costs was only partly offset by significant negative currency effects. Operating expenses decreased 15% to € 454 million from € 535 million in 2017, reflecting a decrease in operating overhead costs. Operating expenses as a percentage of sales declined 0.3 percentage points to 27.8% (2017: 28.1%). As a result of lower operating expenses as a percentage of sales and the gross margin increase, the operating margin improved 3.0 percentage points to 17.1% from 14.0% in 2017. Operating profit in Latin America increased 4% to € 279 million versus € 268 million in 2017. [SEE TABLE 94](#)

**EMERGING MARKETS**

Revenues in Emerging Markets were down 3% on a currency-neutral basis. In euro terms, sales in Emerging Markets **Net sales in Emerging Markets** declined 12% to € 1.144 billion from € 1.300 billion in 2017. Sales of the adidas brand decreased 4% on a currency-neutral basis, driven by single-digit sales decreases in Sport Inspired and, to a lesser extent, Sport Performance. Reebok brand revenues in Emerging Markets remained stable on a currency-neutral basis, as exceptional double-digit growth in Classics was offset by a high-single-digit decline in Sport. [SEE TABLE 95](#)

(3%  
C.N.  
€ 1.144 bn

**Emerging Markets at a glance** € in millions

95

	2018	2017	Change	Change (currency-neutral)
Net sales	1,144	1,300	(12%)	(3%)
adidas brand	1,010	1,153	(12%)	(4%)
Reebok brand	134	147	(9%)	0%
Gross margin	52.8%	49.2%	3.6pp	–
Segmental operating profit	318	325	(2%)	–
Segmental operating margin	27.8%	25.0%	2.8pp	–

Gross margin in Emerging Markets increased 3.6 percentage points to 52.8% (2017: 49.2%), driven by an improved pricing and channel mix as well as lower input costs, partly offset by significant negative currency effects. Operating expenses were down 9% to € 286 million versus € 315 million in 2017, reflecting a decrease in marketing expenditure as well as operating overhead costs. As a percentage of sales, operating expenses increased 0.7 percentage points to 25.0% from 24.2% in 2017. The operating margin was up 2.8 percentage points to 27.8% (2017: 25.0%), as a result of the higher gross margin, which more than offset the negative effect of higher operating expenses as a percentage of sales. Operating profit in Emerging Markets decreased 2% to € 318 million versus € 325 million in 2017. [SEE TABLE 95](#)

# OUTLOOK

In 2019, we expect growth of the global economy and consumer spending to moderate slightly, yet still to provide a positive backdrop for robust 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 significant revenue growth and strong bottom-line improvements in 2019. We forecast sales to increase at a rate between 5% and 8% on a currency-neutral basis. Gross margin is projected to increase to a level around 52.0%, while operating margin is expected to increase between 0.5 percentage points and 0.7 percentage points to a level between 11.3% and 11.5%. As a result, we project net income from continuing operations, excluding the impact from the application of the new reporting standard IFRS 16, to increase between 10% and 14% to a level between € 1.880 billion and € 1.950 billion.

## 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.

## GLOBAL ECONOMIC GROWTH TO SLOW IN 2019<sup>1</sup>

Global GDP growth is projected to moderate slightly to 2.9% in 2019, not least due to a decrease in industrial activity and trade. Furthermore, ongoing trade disputes could become more widespread, adversely affecting economies involved and leading to negative global spillovers. In addition, the global GDP growth projection conceals differences between the pace of growth in developed and developing economies. Developing economies are forecast to see a stabilization of growth at 4.2%, as commodity-exporting economies are expected to benefit from a continued stabilization of oil and other commodity prices. In contrast, growth in developed economies is projected to slow to 2.0%, as further gradual monetary tightening appears likely and capacity constraints become increasingly binding. On a global level, additional downside risks include a rise in borrowing costs and financial market turbulences. Furthermore, ongoing instances of trade protectionism or geopolitical conflicts might dampen consumer confidence, trade and growth.

## SPORTING GOODS INDUSTRY EXPANSION TO CONTINUE IN 2019

In the absence of any major macroeconomic shocks, we expect the global sporting goods industry to grow at a mid-single-digit rate in 2019. North America, the biggest market by size globally, will continue to drive the industry growth in absolute terms. At the same time, most markets globally look set to continue expanding at robust rates. Progressing urbanization and a growing middle class in many developing economies are predicted to further contribute to a growing industry. 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' [SEE GLOSSARY](#)) has become a structural component of the broader fashion landscape, fueling the demand for athletic casual and activewear products. Collaborations between sportswear brands and non-athlete influencers are tending to intensify and multiply. 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 and inventory levels 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. For the sporting goods industry, too, risks related to trade protectionism and geopolitical tensions might intensify.

## CURRENCY-NEUTRAL SALES TO INCREASE BETWEEN 5% AND 8% IN 2019

We expect sales to increase at a rate between 5% and 8% on a currency-neutral basis in 2019. [SEE TABLE 96](#) 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. 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.

## CURRENCY-NEUTRAL REVENUES TO INCREASE IN ALL MARKET SEGMENTS

In 2019, we expect currency-neutral revenues to increase in all market segments. While currency-neutral sales are

<sup>1</sup> Source: World Bank Global Economic Prospects.

projected to grow at a double-digit rate in Asia-Pacific, currency-neutral revenues in North America and Emerging Markets are expected to grow at a high-single-digit rate. Sales in Latin America and Russia/CIS are forecast to improve at a low-single-digit rate in currency-neutral terms. In Europe, we expect to return to growth in the course of the year and forecast a slight increase in currency-neutral revenues in 2019. [SEE TABLE 96](#)

### GROSS MARGIN EXPECTED TO INCREASE

In 2019, the gross margin is forecast to increase to a level around 52.0%. [SEE TABLE 96](#) Gross margin will benefit from the positive effects of favorable currency movements as well as a better channel and regional mix. These improvements will be largely offset by a less favorable pricing mix due to selective price investments, the negative impact from higher labor

expenditures in our sourcing countries and higher commodity prices.

### OPERATING MARGIN TO EXPAND TO A LEVEL BETWEEN 11.3% AND 11.5%

In 2019, the operating margin is expected to increase between 0.5 percentage points and 0.7 percentage points to a level between 11.3% and 11.5% compared to the prior year level of 10.8%. This, together with continued top-line growth, is expected to drive a double-digit-rate improvement of the bottom line. Excluding the impact from the application of the new reporting standard IFRS 16, net income from continuing operations is projected to increase to a level between € 1.880 billion and € 1.950 billion, reflecting an increase of between 10% and 14% compared to the prior year level of € 1.709 billion.

### NEW REPORTING STANDARD TO IMPACT REPORTED EARNINGS

The change in recognition of lease obligations with the first-time application of IFRS 16 as of January 1, 2019, will impact reported earnings. Based on lease contracts as of January 1, 2019, the new reporting standard is projected to have a negative impact of around € 35 million on the company's net income from continuing operations. Including this accounting effect, net income from continuing operations is currently expected to increase to a level between € 1.845 billion and € 1.915 billion. This equals a year-on-year increase of between 8% and 12% compared to the prior year level of € 1.709 billion. [SEE NOTE 01, P. 155](#)

### AVERAGE OPERATING WORKING CAPITAL AS A PERCENTAGE OF SALES TO INCREASE SLIGHTLY

In 2019, average operating working capital as a percentage of sales is projected to slightly increase compared to the significantly better-than-expected prior year level of 19.0%.

### CAPITAL EXPENDITURE TO INCREASE TO UP TO € 900 MILLION

In 2019, capital expenditure is expected to increase to up to € 900 million (2018: € 794 million). Investments will mainly focus on controlled space initiatives of the adidas and Reebok brands in both e-commerce and physical retail, the company's IT and logistics infrastructure as well as the further development of state-of-the-art corporate facilities in Herzogenaurach, Germany, and Portland, Oregon/USA.

#### 2019 Outlook

%

Currency-neutral sales development (in %):	
adidas	to increase at a rate between 5% and 8%
Europe <sup>1</sup>	slight increase
North America <sup>1</sup>	high-single-digit increase
Asia-Pacific <sup>1</sup>	double-digit increase
Russia/CIS <sup>1</sup>	low-single-digit increase
Latin America <sup>1</sup>	low-single-digit increase
Emerging Markets <sup>1</sup>	high-single-digit increase
Gross margin	to increase to a level of around 52.0%
Operating margin	to increase between 0.5pp and 0.7pp to a level between 11.3% and 11.5%
Net income from continuing operations <sup>2</sup>	to increase at a rate between 10% and 14% to a level between € 1.880 billion and € 1.950 billion
Average operating working capital in % of sales	slight increase
Capital expenditure	to increase to a level of up to € 900 million

<sup>1</sup> Combined sales of the adidas and Reebok brands.

<sup>2</sup> 2019 excluding negative impact from accounting change according to IFRS 16 of around € 35 million (based on lease contracts as per January 1, 2019); including this impact, net income from continuing operations is currently expected to increase at a rate between 8% and 12% to a level between € 1.845 billion and € 1.915 billion.

**MANAGEMENT TO PROPOSE DIVIDEND OF € 3.35**

As a result of the strong operational and financial performance in 2018, our robust 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 € 3.35 per dividend-entitled share for 2018 (2017: € 2.60) to shareholders at the Annual General Meeting (AGM) on May 9, 2019. This represents a payout ratio of 39.0% based on the company's net income from continuing operations (2017: 37.0%). This is 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 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 97](#) 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.

Working independently of all other functions of the organizations, the Internal Audit department provides objective assurance to the Executive Board and the Audit Committee 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.

Our risk and opportunity management system is based on 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 (at least 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 growth at a local and global level. Equally, our analysis

adidas risk and opportunity management system

97



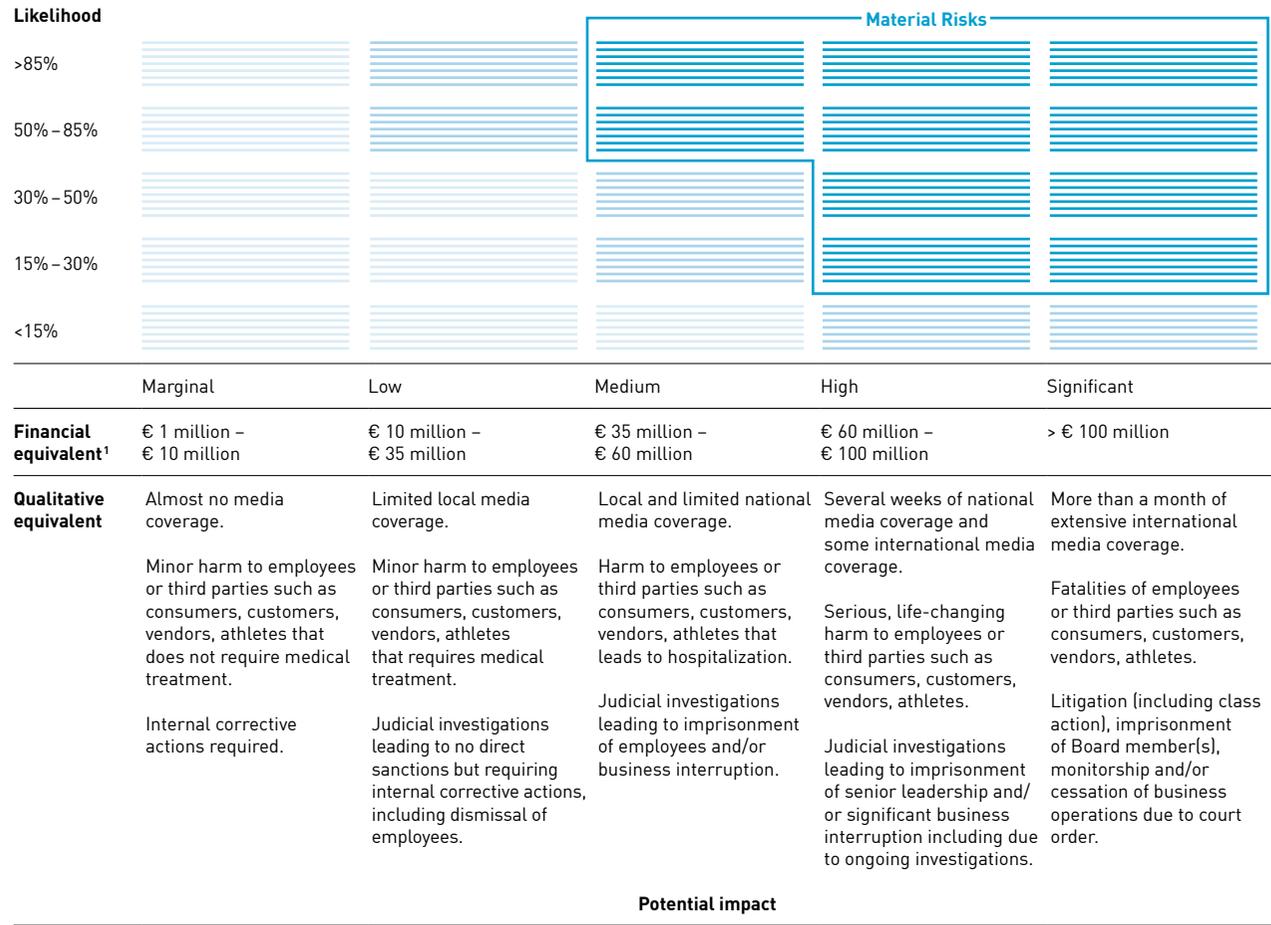
focuses on those areas that are at risk of saturation or exposed to increased competition or changing consumer tastes. However, our risk and opportunity identification process is not only limited to external risk factors or opportunities; it also includes an internal perspective that considers company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

- **Risk and opportunity evaluation:** We assess 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 three categories: minor, moderate and major (previously: marginal, minor, moderate, significant, major).

The potential impact is evaluated using five categories: marginal, low, medium, high and significant. These categories represent financial or equivalent non-financial measurements. The financial measurements are based on the potential effect on the company’s net income. Non-financial measurements used are the degree of media exposure affecting the company’s reputation, brand image and employer value proposition, the degree of damage to people’s health and safety, and the degree of legal and judicial consequences at the corporate and personal level. 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: below 15%, 15% - 30%, 30% - 50%, 50% - 85% and above 85%.

SEE DIAGRAM 98

Risk evaluation categories



Risk classification: Minor Moderate Major  
<sup>1</sup> Based on net income.

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 risk before any mitigating action, the net risk reflects the residual 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 major 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 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. The Executive Board sets the tone right from the top – 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 around 57,000 employees, however, we realize that it will never be possible to exclude compliance violations with absolute certainty.

The adidas Fair Play Compliance Framework is overseen by the company's Chief Compliance Officer. We see compliance as all-encompassing, spanning all business functions throughout the entire value chain. Our central Compliance team works closely with Regional Compliance Managers and Local Compliance Officers to conduct a systematic assessment of key compliance risks on a yearly basis. In addition, the central Compliance team regularly conducts compliance reviews within selected entities.

The company's Compliance Management System (CMS) 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; and
- preserve diversity by fighting harassment and discrimination.

The adidas Fair Play Code of Conduct stipulates guidelines for behavior in everyday work, which all employees are obliged to comply with. It is applicable globally and for all business areas, accessible on our website and on our intranet. In 2018, we improved the usability of the Code of Conduct and refreshed its design. We also consolidated five compliance policies into one user-friendly Compliance Policy that covers topics including Anti-Bribery and Corruption, Gifts and

Entertainment, Anti-Fraud and Theft, Antitrust and Competition Law, Conflict of Interests, Non-Retaliation, and Consequence Management. [ADIDAS-GROUP.COM/S/CODE-OF-CONDUCT](https://www.adidas-group.com/s/code-of-conduct)

The Code of Conduct and our CMS are organized around three pillars: prevent, detect and respond.

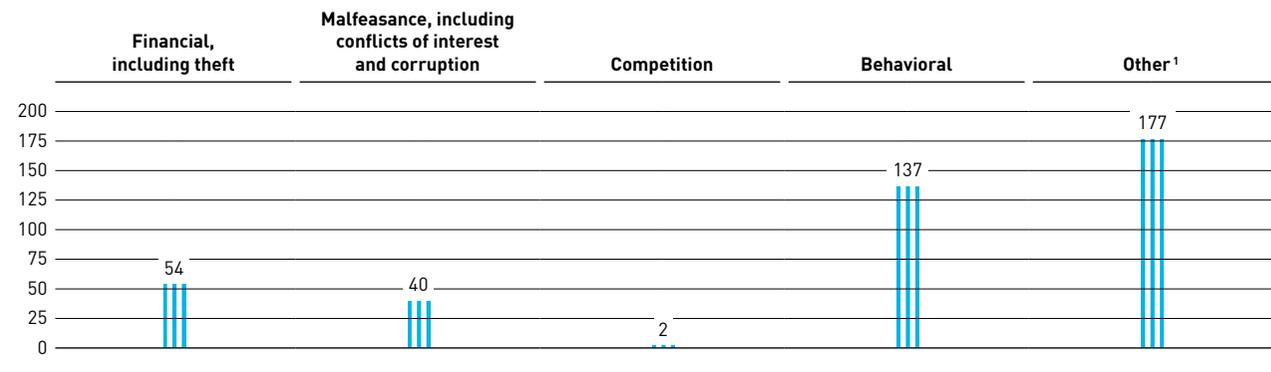
- **Prevention:** The foundation of our CMS is the adoption and implementation of our Fair Play Code of Conduct, the Compliance Policy, and the Privacy Policy. adidas issues targeted compliance-related communication by management and the Compliance department and provides mandatory training to all employees globally during onboarding as well as in regular, repeated cycles. In 2018, we updated the online Code of Conduct training, which more than 18,000 employees completed. Additionally, nearly 18,000 employees completed our web-based Preventing Fraud and Theft training. Furthermore, we conducted in-person compliance training seminars with members of the Executive Board, senior management and newly promoted or hired senior executives across the

globe in order to further enhance the compliance 'tone from the top', as well as the 'tone from the middle'. We closely monitor the completion rates for these training measures and continuously update our web-based training.

- **Detection:** We implemented whistleblowing procedures to ensure timely detection of potential infringements of statutory regulations or internal guidelines. Employees can report compliance concerns internally to their supervisor, the Chief Compliance Officer, Regional Compliance Managers or Local Compliance Officers, the relevant HR manager or the Works Council. Employees can also report externally via an independent, confidential reporting hotline, website, or email service, and can choose to do so anonymously through the Fair Play hotline. The hotline is available at all times worldwide.
- **Response:** Appropriate and timely response to compliance violations is essential. The Chief Compliance Officer leads all investigations in cooperation with an established team of Regional Compliance Managers and a global network of Local Compliance Officers. We track, monitor, and report

Potential compliance violations

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<sup>1</sup> Includes payroll issues, intellectual property and leaks of confidential information, inter alia.

potential incidents of non-compliance worldwide. In 2018, we recorded 410 potential compliance violations (2017: 419). [SEE DIAGRAM 99](#), [SEE DIAGRAM 100](#) Most importantly, insights gained from the investigation of past violations are used to continuously improve the CMS. Where necessary, we react promptly to confirmed compliance violations, through appropriate and effective sanctions ranging from warnings to termination of employment contracts.



In 2018, we reinforced the adidas compliance organization and activities, and enhanced cooperation with other governance functions, e.g. Internal Audit, Internal Controls, and Risk Management.

The company's General Counsel and the Chief Compliance Officer regularly report to the Executive Board on the further development of the compliance program and on major compliance cases. In addition, the Chief Compliance Officer reports to the Audit Committee on a regular basis. In 2018, the Chief Compliance Officer attended five meetings of the Audit Committee of the Supervisory Board to report on the further development of the compliance program, major compliance cases and other relevant compliance topics. [▶](#)

### 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, assess, limit and control risks identified in the consolidated financial reporting process which might result in the 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. 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 assesses the effectiveness of selected

internal controls, including IT controls. 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. 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.

### ILLUSTRATION OF RISKS

This report includes an explanation of risks that we deem to be relevant to the achievement of the company's objectives in the time period from 2019 to 2021. According to our risk assessment methodology, only consumer demand risks, business partner risks and risks related to customs and tax regulations are considered material. Our presentation of risks in this year's Annual Report differs slightly from the 2017 Annual Report as we have adjusted financial and non-financial measurements to assess the potential impact. The risks overview table shows the assessment of all risks described below. [SEE TABLE 101](#)

### STRATEGIC RISKS

#### Consumer demand risks

Success in the sporting goods industry largely depends on the ability to continuously create new, innovative footwear and apparel products. In that respect, anticipating and quickly responding to changes in consumer demand or consumer trends is essential. Consumer demand changes can be sudden and unexpected, particularly when it comes to the more fashion-related part of our business. 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, especially considering our strategy to focus on key product franchises. [SEE ADIDAS BRAND STRATEGY, P. 67](#) Because of average lead times of 12 to 18 months, we face a risk of short-term revenue loss

#### Corporate risks overview

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	Potential impact	Change (2017 rating)	Likelihood	Change (2017 rating)
<b>Strategic risks</b>				
Consumer demand risks	High	↓ (Significant)	15%–30%	
Risks related to distribution strategy	Medium	↓ (Significant)	30%–50%	
Macroeconomic, sociopolitical and regulatory risks	Significant		< 15%	
Competition risks	Medium		15%–30%	↓ (30%–50%)
Risks related to technology change	Medium	↓ (High)	15%–30%	
<b>Operational risks</b>				
Business partner risks	High	↓ (Significant)	15%–30%	
IT and cyber security risks	Significant	↑ (High)	< 15%	↓ (15%–30%)
Hazard risks	Significant		< 15%	
Project risks	Significant		< 15%	
Inventory risks	Medium	↓ (High)	15%–30%	↑ (< 15%)
Personnel risks	Medium	↓ (High)	< 15%	
<b>Legal and compliance risks</b>				
Risks related to customs and tax regulations	High		15%–30%	↓ (30%–50%)
Risks related to product counterfeiting and imitation	Significant		< 15%	↓ (15%–30%)
Fraud and corruption risks	Significant		< 15%	
Data privacy risks	High	↓ (Significant)	< 15%	↓ (15%–30%)
<b>Financial risks</b>				
Currency risks	Significant		< 15%	↓ (15%–30%)
Credit risks	Significant		< 15%	

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. By putting the consumer at the center of our decision-making we intend to create higher brand advocacy. As part of our adidas brand advocacy program, we continuously monitor the *Net Promoter Score (NPS)* [SEE GLOSSARY](#) and strive to understand consumers' perception. [SEE ADIDAS BRAND STRATEGY, P. 67](#) 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. Our Speed programs also help us mitigate the risk as they enable us to be faster in case of demand shifts. [SEE CORPORATE STRATEGY, P. 62](#) By leveraging our promotion partnerships for launches of key product franchises and by carefully orchestrating launch events across markets and channels, we intend to maintain brand desire and consumer demand at a constantly high level. Our collaboration-based innovation model Open Source also helps us to utilize external insights to drive consumer demand, brand desire, market share and profitability.

### Risks related to distribution strategy

The retail industry has seen continuous change over the last few years, with consumers demanding a seamless shopping experience across various distribution channels. The inability to adjust our distribution strategy in a timely manner to this changing retail industry, which is experiencing increasing substitution of physical retail stores by digital commerce platforms as well as an increasing connection of physical and digital retail, could result in sales and profit shortfalls. A decline in the attractiveness of particular shopping locations such as shopping malls could lead to sales shortfalls in our customers' and our own stores, higher inventory in the marketplace, increased clearance activity and margin pressure. 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. 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.

To mitigate these risks, adidas has developed and implemented clearly defined distribution policies and procedures to avoid overdistribution of products in a particular channel. We continuously and closely monitor numerous indicators (e.g. order placement, sell-through rates at point of sale, average selling prices, discounts, store traffic) that help us identify changes in the retail environment and quickly take appropriate action such as closing or remodeling own stores. New store openings are managed according to a standardized company-wide business plan model, taking into account best practices from around the world. We constantly adjust our segmentation strategies to ensure that the right product is sold at the right

point of sale to the right consumer at an appropriate price. Our omni-channel initiatives help us leverage learnings across our distribution channels and prevent cannibalization.

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

### Macroeconomic, sociopolitical and regulatory risks

Growth in the sporting goods industry is highly dependent on consumer spending and consumer confidence. Economic downturns, financial market turbulence 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, regulations concerning product safety) could lead to potential sales shortfalls or cost increases. For example, the UK's withdrawal from the European Union ('Brexit') could cause business and consumer uncertainty and create an additional administrative burden to adhere to changes in regulatory frameworks concerning critical areas such as the movement of goods or the movement of people. The ongoing trade dispute between the US and China could result in the imposition of additional trade tariffs also affecting athletic footwear and apparel and could have substantial effects on economic growth not only in two of the company's key markets but also globally.

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 manufacturing of our products to alternative countries, 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. For example, to best serve the UK market after 'Brexit' and minimize business disruption resulting from potentially more burdensome customs procedures, we have pro-actively adjusted our supply chain and logistics set-up by increasing our distribution capacity in the UK and reducing the portion of cross-border shipments from the EU. 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.

### Competition risks

Strategic alliances amongst competitors and/or retailers, the increase in retailers' own private label businesses and intense competition for consumers, production capacity and promotion partnerships between well-established industry peers and new market entrants 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.

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 (e.g. product launches, selective pricing adjustments)

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 the German Football Association (DFB) or James Harden, as well as adding new partners to refresh and diversify our portfolio, e.g. Paulo Dybala or Cardi B. In addition, our product and communication initiatives are designed to increase brand desire, drive market share growth and strengthen our brands' market position.

### 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, 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. We have established processes for technology scouting and technology lifecycle management which ensure a continuous assessment of the technology landscape and timely replacement of outdated technology. Furthermore, we build partnerships with technology and business leaders around the world such as BASF, Carbon or Oechsler to stay connected to the latest advancements. ■ [SEE INNOVATION, P. 78](#)

## OPERATIONAL RISKS

### Business partner risks

adidas interacts and enters into partnerships with various third parties, such as athletes, creative partners, innovation partners, retail partners or suppliers of goods or services. 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 on the part of business partners

or improper behavior of individual athletes, influencers or partners in the entertainment industry could have a negative spill-over effect on the company's reputation, lead to higher costs or liabilities or even 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 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 as well as entertainers and influencers 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 2018. To reduce risk 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 in different countries and, for the vast majority of its products, does not have a *single-sourcing model*.

[SEE GLOSSARY](#)

### IT and cyber security risks

Theft, leakage, corruption or unavailability of critical information (e.g. consumer data, employee data, product data) could lead to reputational damage, regulatory penalties or the inability to perform key business processes. Key business processes, including product marketing, order management, warehouse management, invoice processing, customer support and financial reporting, are all dependent on IT systems. Significant outages, application failures or cyber security threats to our infrastructure, or that of our business partners, could therefore result in considerable business disruption or impact to business-critical data.

To mitigate these risks, our IT organization proactively engages in system preventive maintenance, service continuity planning, adherence to applicable IT policies and maintenance of a comprehensive information security program. Information security governance, data security, security architecture design, continuity management and employee awareness programs are aligned with industry-best practices in order to protect the company adequately.

### Hazard risks

adidas is exposed to external risks such as natural disasters, unfavorable or extreme weather conditions, epidemics, fire, accidents and malicious acts. Those events may cause physical damage to our own or our suppliers' premises, production units, warehouses and stock in transit and result in business interruption. In addition, any such event could threaten the safety or security of our employees.

To minimize potential negative effects, we have secured insurance coverage for property damage and business interruption and implement loss prevention (e.g. sprinklers in facilities) and contingency plans to quickly recover business activities. We also work with reliable suppliers and logistics providers who guarantee high safety standards in their facilities. In addition, we are strengthening our own safety and security measures worldwide by establishing global and local policies as well as standardized processes and common systems for safety and security management.

### Project risks

To effectively support further business growth and improve efficiency, adidas continuously invests in new projects such as the creation, implementation, expansion or harmonization of IT systems and distribution centers or the construction of office buildings. Ineffective project management could delay the execution of critical projects and lead to higher expenditures. Inadequate project planning and controlling as well as executional mistakes could cause inefficiencies, delays or business disruption, resulting in higher costs and sales shortfalls. Inappropriate project governance, prioritization and oversight of the project portfolio may lead to suboptimal resource allocation and undesired project results.

We manage projects utilizing reviews by project teams as well as project steering committees to evaluate the progress, quality and costs of those projects on a regular basis. This approach allows early detection of project risks and quick implementation of corrective action or timely cancellation of projects with a low chance of success. To ensure true end-to-end management of key projects we have established a network of program and project management departments across all main functions (i.e. Sales, Marketing, Operations, Finance, IT and Human Resources). We also work with external partners for project management support in areas where we do not have the required expertise or experience in-house.

### 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. [SEE INTERNAL MANAGEMENT SYSTEM, P. 103](#) 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 choice 'Speed' is an important driver, enabling 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](#)

### 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, ineffective leadership as well as the failure to install and maintain a performance-oriented culture that fosters diversity and inclusion and 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 highly qualified and skilled talents who best meet the specific needs of our company pose 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 is an essential part of our strategic business plan 'Creating the New' and is designed to reduce these risks. To optimize staffing levels and resource allocation (i.e. having the right people with the right skillsets in the right roles at the right time), we have established a strategic workforce management process. 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 established a global recruiting organization to enhance our internal and external recruiting services and capabilities. To ensure effective leadership across the company, we defined and activated our global *Leadership Framework* [SEE GLOSSARY](#) that articulates the behaviors expected of our leaders. Our global succession management helps create strong internal talent pipelines for critical leadership positions and reduce succession risk. We also strengthen employee retention by providing attractive

leadership development and learning programs as well as global career opportunities. Numerous initiatives such as our global 'BIG Deal' gender intelligence training foster diversity and inclusion. We also have attractive reward and incentive schemes in place, designed to further support long-term employee commitment. [SEE PEOPLE AND CULTURE, P. 81](#)

### LEGAL AND COMPLIANCE RISKS

#### 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.

### 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. We have also stepped up product security labeling with our authorized suppliers.

### Fraud and corruption risks

We face the risk that members of top management 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.

### 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 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.

To mitigate these risks, we have established a global privacy management policy that outlines the company's privacy principles and provides the framework for the use of personal information. In addition, we have implemented a global deletion policy that governs the deletion of personal information at adidas. These policies apply to all adidas businesses worldwide and set our expectations of third-party business partners for managing personal information for or on behalf of adidas. Our global privacy officer and the global privacy department are establishing a monitoring framework to track and report adherence to data protection and privacy standards. They are continuously providing further implementation guidance and training. We are also working with external partners and law firms to ensure we are informed about legal requirements across the globe, and we take appropriate action to ensure compliance.

## FINANCIAL RISKS

### Currency risks

Currency risks for adidas are a direct result of multi-currency cash flows within the company, in particular the mismatch of the currencies required for sourcing our products versus the denominations of our sales. 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. [SEE NOTE 31, P. 194](#)

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-months horizon.

[SEE TREASURY, P. 115](#)

### Credit risks

A credit risk arises if a customer or other counterparty to a financial instrument fails to meet its contractual obligations. [SEE NOTE 31, P. 194](#) adidas is exposed to credit risks from its operating activities and from certain financing activities. Credit risks arise principally from accounts receivable and from other third-party contractual financial obligations.

We analyze the creditworthiness of our customers and establish tolerance limits for accounts receivable. 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.

adidas subsidiaries are typically only authorized to work with banks rated BBB+ or higher. [SEE TREASURY, P. 115](#) We monitor credit default swap premiums of our partner banks on a monthly basis and shift credit balances to banks compliant with our limits if a defined threshold is exceeded.

## ILLUSTRATION OF OPPORTUNITIES

In this report, we illustrate opportunities considered material in the time period from 2019 to 2021. Our presentation of opportunities in this year's Annual Report differs slightly from the 2017 Annual Report as we have adjusted financial and non-financial measurements to assess the potential impact. The assessment is shown in the opportunities overview table.

■ SEE TABLE 102

### 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. This includes the further expansion of our own e-commerce activities, the optimization of our network of wholesale

partners with a clear focus on partners that provide consumers with the best shopping experience and customer service, retail space management with key accounts (online and brick & mortar), 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

**Product portfolio:** 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. The further expansion of our women's business could result in additional market share and net sales growth and lead to further profitability improvements.

**Major sports events:** Major sports events such as the upcoming Olympic Summer Games in Tokyo provide adidas with an ideal platform to showcase its strength as a sports brand and demonstrate its role as a leader in innovation to a worldwide audience. In addition, a major sports event also always represents a commercial opportunity in the host country which typically benefits from the influx of foreign tourists and increased consumer spending. As a result, we see potential for additional sales growth and consequently stronger bottom-line performance in connection with major sports events.

#### 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 Data & Analytics team to drive business decision-making by leveraging the power of data. The continuous enhancement of our existing capabilities to build and scale insights-driven use cases and the use of the latest technology could bring value to our business operations across the entire company. As a result, we see the opportunity to 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

#### Corporate opportunities overview

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	Potential impact	Change (2017 rating)	Likelihood	Change (2017 rating)
<b>Strategic and operational opportunities</b>				
Organic growth opportunities	High	↓ [Significant]	15% – 30%	
Opportunities related to organizational and process improvements	High		15% – 30%	↓ [30% – 50%]
Macroeconomic, sociopolitical and regulatory opportunities	High		> 85%	
<b>Financial opportunities</b>				
Favorable financial market changes	Significant		15% – 30%	

**Macroeconomic, sociopolitical and regulatory opportunities**

Legislative and regulatory changes such as the elimination of trade barriers due to free trade agreements (e.g. between the European Union and Vietnam) can create cost savings or potentially open up new channels of distribution and, as a result, positively impact profitability. Changes in local tax or customs regulations (e.g. reduction of tax rates on private incomes, reduction of import duties) could lead to increased consumer spending and consequently positively affect our sales or result in additional cost savings.

**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](#)

# 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 2018, 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. 106](#) The continued 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 significant sales growth and strong profitability improvements throughout the year. While some company-specific weaknesses in our home market Europe led to a slight downward revision of our top-line guidance in November 2018, we were able to increase our bottom-line guidance at the same time. The better-than-expected profitability increase was largely driven by the strong gross margin improvement, which reflects the high quality of our revenue growth. [SEE TABLE 103](#)

In 2018, revenues increased 8% on a currency-neutral basis, driven by double-digit growth in North America and Asia-Pacific. Revenues in Europe and Emerging Markets grew at a lower rate than initially expected, which led to a revenue increase at the lower end of our initial guidance range of around 10% currency-neutral sales growth. Gross margin increased 1.4 percentage points to 51.8%, significantly

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, channel and product mix as well as lower input costs, which more than offset strong headwinds from unfavorable currency movements. The operating margin increased 1.1 percentage points to a level of 10.8%, which was above our initial guidance of an increase of between 0.5 and 0.7 percentage points. This development was mainly due to the gross margin increase, which more than offset an increase in other operating expenses as a percentage of sales. The increase in other operating expenses as a percentage of sales, compared to our initial expectation of a slight decline, was driven by additional investments into marketing and scalability initiatives that were funded by the better-than-expected gross margin development. As a result, net income from continuing operations was up 20% to € 1.709 billion, excluding the negative one-time tax impact in 2017, and thus exceeded our initial guidance of an improvement at a rate between 13% and 17%. [SEE INCOME STATEMENT, P. 107](#)

In 2018, average operating working capital as a percentage of sales ended the year at a level of 19.0%. This development represents a significant decrease compared to the prior year level of 20.4%, while our initial guidance was for a largely stable year-over-year development. The better-than-expected development mainly reflects the company's successful efforts on tightening working capital management. Capital expenditure amounted to € 794 million in 2018, below our initial guidance of around € 900 million, 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 both in own e-commerce and our stores, 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. 103](#) In 2018, our Net Promoter Score (NPS) saw further improvements, reflecting the strength of our brands. [SEE](#) 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](#) Our diligence and discipline in sustainability matters continues to yield strong recognition for our company. In 2018, adidas AG was again represented in a variety of high-profile sustainability indices. For the 19th 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. adidas received 'Gold Class' distinction for its excellent sustainability performance and was rated as overall leader in the 'Textiles, Apparel & Luxury Goods' industry, receiving industry-best scores in criteria including Human Rights, Supply Chain Management, Innovation Management, and Operational Eco-Efficiency. [SEE SUSTAINABILITY, P. 88](#) As we are convinced that our employees' feedback plays a crucial role in our pursuit of creating a desirable work environment, in 2018 we fully embedded 'People Pulse', our approach and system platform for a quarterly measurement of the level of employee satisfaction, within the organization globally. We saw People Pulse gain significant traction, with participation rates toward year-end exceeding our minimum participation rate target. [SEE PEOPLE AND CULTURE, P. 81](#)

Finally, despite some challenges in the North American market, we continue to enjoy an overall strong level of on-time in-full (OTIF) deliveries to our customers and own-retail stores. In 2018, OTIF remained stable compared to the prior year level. [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. As a result of these changes, we believe the overall adidas risk profile has improved slightly compared to the prior year.

### Company targets versus actual key metrics

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	2017 Results <sup>1</sup>	2018 Initial targets <sup>1,2</sup>	2018 Updated targets <sup>1,3</sup>	2018 Results <sup>1</sup>	2019 Outlook
Sales (year-over-year change, currency-neutral)	16%	to increase at a rate of around 10%	to increase at a rate between 8% and 9%	8%	to increase at a rate between 5% and 8%
Gross margin	50.4%	to increase up to 0.3pp	to increase up to 1.0pp	51.8% 1.4pp	to increase to a level of around 52.0%
Other operating expenses <sup>4</sup> (in % of net sales)	41.3%	below prior year level	below prior year level	41.9% 0.5pp	–
Operating profit (€ in millions)	2,070	to increase at a rate between 9% and 13%	to increase at a rate between 12% and 16%	2,368 14%	–
Operating margin	9.8%	to increase between 0.5pp and 0.7pp	to increase around 1.0pp	10.8% 1.1pp	to increase between 0.5pp and 0.7pp to a level between 11.3% and 11.5%
Net income from continuing operations <sup>5,6</sup> (€ in millions)	1,430	to increase at a rate between 13% and 17%	to increase at a rate between 16% and 20%	1,709 20%	to increase at a rate between 10% and 14% to a level between € 1.880 billion and € 1.950 billion
Basic earnings per share from continuing operations <sup>5</sup> (in €)	7.05	to increase at a rate between 12% and 16%	to increase at a rate between 15% and 19%	8.46 20%	–
Average operating working capital (in % of net sales)	20.4%	around prior year level	around prior year level	19.0% (1.4pp)	slight increase
Capital expenditure <sup>7</sup> (€ in millions)	752	around € 900 million	around € 900 million	794 6%	to increase to a level of up to € 900 million

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

<sup>2</sup> As published on March 14, 2018.

<sup>3</sup> As published on November 7, 2018.

<sup>4</sup> Figures reflect the adjusted consolidated income statement structure introduced in 2018.

<sup>5</sup> 2017 excluding negative one-time tax impact of € 76 million.

<sup>6</sup> 2019 excluding negative impact from accounting change according to IFRS 16 of around € 35 million (based on lease contracts as per January 1, 2019); including this impact, net income from continuing operations is currently expected to increase at a rate between 8% and 12% to a level between € 1.845 billion and € 1.915 billion.

<sup>7</sup> Excluding acquisitions and finance leases.

## 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 are expected to 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 income from continuing operations to expand by 20% to 22% on average per year during the five-year period, we once again upgraded our long-term profitability target in March 2018 following the strong operational and financial performance in 2017. As a result, we expect net income from continuing operations to grow by 22% to 24% on average per year. [SEE CORPORATE STRATEGY, P. 62](#)

Against the background of rising consumer spending, increasing penetration of sportswear ('athleisure') and growing health awareness in most geographical areas, we project further top-line improvements in 2019. The revenue increase is to be driven by our extensive pipeline of new product launches paired with brand-building activities. 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 the sales growth. In combination with tight control of inventory levels and stringent cost management, we expect to once again generate profitability improvements in 2019. Supported by a further expansion in gross and operating margin, our net income is expected to improve strongly in 2019. [SEE OUTLOOK, P. 128](#) We believe that our outlook for 2019 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 further top- and bottom-line improvements in 2019. 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. 106](#) No other material event between the end of 2018 and the publication of this report has altered our view.

# CONTACT

**ADI-DASSLER-STR. 1  
91074 HERZOGENAURACH  
GERMANY**

TEL + 49 (0) 91 32 84 - 0  
FAX + 49 (0) 91 32 84 - 22 41  
➤ ADIDAS-GROUP.COM

**ADIDAS IS A MEMBER OF DIRK**  
(GERMAN INVESTOR RELATIONS  
ASSOCIATION)

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## **INVESTOR RELATIONS**

TEL + 49 (0) 91 32 84 - 29 20  
FAX + 49 (0) 91 32 84 - 31 27

➤ [INVESTOR.RELATIONS@ADIDAS-GROUP.COM](mailto:INVESTOR.RELATIONS@ADIDAS-GROUP.COM)  
➤ [ADIDAS-GROUP.COM/INVESTORS](http://ADIDAS-GROUP.COM/INVESTORS)

## **PHOTO CREDITS**

ADIDAS, ANDREAS KÜCHENMEISTER  
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