**RISKS FROM RISING INPUT COSTS** Raw material and labor costs account for approximately 70 % of the Group's cost of sales. Prices of materials such as rubber, which closely correlate with the oil price, are especially subject to the risk of price increases. As our ordering process and price negotiations usually take place around six months in advance of production, our sourcing function has visibility and reaction time to manage and plan for sharp increases in input costs.

To reduce the financial impact on our product margins from higher sourcing costs, we collaborate closely with our vendors to increase efficiency in manufacturing processes and search for new materials. In addition, we have exploited economies of scale from our higher sourcing volume following the Reebok acquisition and are constantly improving production efficiency. see Global Operations, p. 062 We may also compensate for this risk by increasing the selling prices of our products – although this is subject to the prevailing consumer and retail climate. In addition, in the medium term we have the ability to adapt our sourcing structure to take advantage of more competitive pricing in other locations.

We continue to assess the risks from rising input costs as having a medium likelihood. As a result of the time lag between ordering and production, we believe the short-term financial impacts from input cost increases are low. However, with the sharp oil price increases during 2007, ongoing wage inflation in Asia and increasing freight costs, we believe the potential financial impact from rising input costs has grown for the medium term. This could have a medium financial impact on our profitability beyond 2008.

**SUPPLIER DEFAULT RISKS** Over 95 % of our product offering is sourced through independent suppliers mainly located in Asia. see Global Operations, p. 062 To reduce the risk of business interruptions following a potential supplier default, we work with vendors who demonstrate reliability, quality, innovation and continuous improvement. In addition, we have bought insurance coverage for the risk of business interruptions caused by physical damage to supplier premises. The Group has also significantly reduced the number of independent manufacturers by combining the adidas and Reebok sourcing organizations. This exercise has allowed us to reduce risk by simplifying our sourcing structure, and focusing on the highest-quality suppliers, without compromising our flexibility or competitiveness.

We continue to assess supplier risks as having a low likelihood of occurrence and potential financial impact.

**PRODUCT QUALITY RISKS** The adidas Group faces a risk of selling defective product, which may result in injury to consumers and / or image impairment. We mitigate this risk through rigorous testing prior to production, close cooperation with suppliers throughout the manufacturing process, random testing after retail delivery, open communication about defective products and quick settlement of product liability claims when necessary. In 2007, approximately 3,400 FSMK hockey masks which were delivered to retail in Canada, Europe and the USA, were subsequently recalled voluntarily due to a quality issue. The issue arose during subsequent random testing of products after market launch. During these random tests, a hockey puck was aimed at full speed directly at the face masks. Many of the masks dented and the coating chipped slightly. No incidents or injuries were reported before or after the recall.

Our assessment of product quality risk remains unchanged versus the prior year. We regard the likelihood of significant product liability cases or having to conduct wide-scale product recalls as low. As we have insurance protecting us against the financial consequences of significant product liability cases, we also assess the financial impact as low.

**CUSTOMER RISKS** Customer risks arise from our dependence on key customers who have the ability to exert bargaining power and can therefore cause considerable margin pressure or cancel orders. These risks exist not only due to the relative size of some of our major customers, but also as a result of our limited ability to impact how they conduct business and the external impacts of the consumer environment in which they operate.

To limit these risks, we utilize a broad distribution strategy which includes our expanding controlled space activities. This enables us to reduce negative consequences that result from sales shortfalls that can occur with key customers. Specifically, no customer at brands adidas, Reebok and TaylorMade-adidas Golf accounted for more than 10 % of brand sales in 2007. In addition, we are proactively cooperating with key retail partners to further optimize sales through innovative point-of-sale initiatives (e.g. our shop-in-shop concepts at Dick's Sporting Goods).

When necessary, we also restrict the distribution of our brands to protect brand image or product margins, and to streamline supply. For example, in the course of 2007, the Group decided to limit the Reebok product offering to an important mall-based key account in North America who had continually discounted Reebok product. Although we have been strengthening Reebok's business in other retail channels such as sporting goods, we expect this development will have a significant negative impact on Reebok segment sales in North America throughout 2008. Nevertheless, the Group projects only a low impact on the Group's overall contribution in 2008 from this action.

Due to the current difficulties at mall-based retailers and the overall economic environment in the USA, we continue to view a strong reduction of business with one of our brands' biggest retailers as having a medium likelihood of occurrence. Such an event could have a medium financial impact on the sales and profitability of a particular region. However, on a Group level, we continue to view the financial impact from customer risks as low.