

fy04



Corporate Responsibility Report



CORPORATE RESPONSIBILITY REPORT: PART I

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The Artwork

Artwork in this report is by young people from inner city Berlin. They participated in programs run by Schlesische 27, a local organization that uses art and culture to engage socially disadvantaged youth.

We worked with S27 and introduced young people to aspiring Olympians their own age. We then asked them to explore – using words, photography and painting – what sport means to them.

Their work moved us. And inspired us.

A Message from Phil Knight

We've been fairly quiet for the past three years in

Corporate Responsibility because of the Kasky lawsuit. So we're using this report to play a little catch-up and draw a more complete picture. It makes for a long report, but I urge you to read it from cover to cover. And then some: because probably the most significant piece of disclosure linked to this report is actually on our Web site. It's a listing of all factories that produce Nike-branded products, worldwide.

Over the last decade, I've seen a number of chapters written on the quest to improve working conditions in the apparel and footwear industry. In the first chapter, we upgraded processes and conditions behind closed doors. However inadequate our critics may have found these efforts, they did result in factories that were far better than what we found originally. It was also in this chapter that the application of water-based cement was started – one that now eliminates a huge percentage of toxic fumes in shoe factories. Also in this chapter was the creation of codes of conduct in shoe factories.

The second chapter began with critics bringing working conditions in underdeveloped countries to the attention of the world. After a bumpy original response, an error for which yours truly was responsible, we focused on making working conditions better and showing that to the world.

These codes led to a third long chapter on the development of corporate and independent monitoring programs. The fourth chapter charts the beginning of collaborative efforts to address compliance issues. Creating change has proved more challenging than anyone imagined when corporate codes were first developed.

This report taught us that to write that next chapter, we and others involved in this discussion are going to need to see common standards emerge and ways to better share knowledge and learnings created. We are disclosing our supply chain in an effort to jump-start disclosure and collaboration throughout the industry.

I said you can't do it alone. I also know that you can't do it forever. Last November, I announced that I was stepping down as CEO (I'll still serve as Chairman of the Board). Bill Perez is the new CEO for Nike, Inc. based, in part, on Bill's track record in corporate responsibility. His philosophy is that companies must invest in and improve their communities. I'll be there to help him any way I can.

Our goal in writing this report has been to be as accurate, complete and honest as we can be about how Nike performs. Just producing this report proved to us that the value of reporting goes far beyond transparency. It becomes a tool for improving both our management of business and in giving us clues about what we need to do next. I have confidence that the Nike team will continue to drive Nike toward our goal of becoming a corporate responsibility leader in 21st century business.

Sincerely,



Philip H. Knight
Founder & Chairman



This report taught us that to write that next chapter, we and others involved in this discussion are going to need to see common standards emerge and ways to better share knowledge and learnings created.



Corporate responsibility challenges us to take a good, hard look at our business model, and understand our impact on the world around us.



A Letter from the Nike Brand Presidents

Corporate responsibility challenges us to take a good, hard look at our business model, and understand our impact on the world around us.

Some of what we see is concerning. As a global company, we have social impacts in every region of the world. Despite our concerted efforts, improving working conditions in our supply chain is still a major challenge. With our aggressive, ongoing monitoring programs, we now believe we have a more accurate picture of where the problems of non-compliance lie. We see four key issues where non-compliance remains a challenge, both in our supply chain and across our industry: freedom of association, hours of work, wages and harassment. These issues will be a focus of our labor efforts moving forward.

There are also environmental impacts. While the “leave no trace” slogan may work for backpackers, it is a challenge for any company or industry operating on a global scale. At every stage of a product’s life cycle – from the gathering of raw materials to the disposal of goods by consumers – there is waste. Here, too, we are gaining a better picture of our footprint and working to live our values.

Some of what we see is thrilling. We continue to be amazed by the capacity of our athletes, partners and employees to inspire people around the world. NikeGO has brought the benefits of physical activity to large numbers of young people; they’re less likely to get into trouble and more likely to be healthy when they’re at play on courts, tracks, fields and pitches. The global supply of organic cotton continues to grow, in part because our demand for it is growing. Then there are the yellow wristbands – more than 33 million sold since we launched the campaign – that help the Lance Armstrong Foundation support those living with cancer.

Understanding our impact leads us to questions of strategy. For our company as a whole, we’ve set three strategic goals:

- To effect positive, systemic change in working conditions within the footwear, apparel and equipment industries;
- To create innovative and sustainable products; and
- To use sport as a tool for positive social change and campaign to turn sport and physical activity into a fundamental right for every young person.

First, we want Nike to play a role in effecting positive, systemic change in working conditions within our industries. If our efforts lead to a workplace oasis – one solitary and shining example in a desert of poor conditions – then we’ve not succeeded. Even if that single shining example were to exist (and we’re not claiming it does), we’ve learned that positive changes won’t last unless the landscape changes. Our challenge is to work with the industry and our contract manufacturers to collectively address these systemic non-compliance issues that our data so highlight. This is one of the key reasons we made the decision to disclose our supply base; we believe this could encourage other companies to do the same. Our belief is that in disclosing, the industry will find ways to better share knowledge and learnings. This, in turn, will facilitate the building of further partnership approaches that are built on best practice and gradually lead us to standard codes, standard approaches to monitoring, standard reporting, standard parameters for transparency. It’s our belief that for market forces to enable responsible competitiveness, consumers must be able to reward brands and suppliers using fact-based information. Compliance efforts need to be optimized, made affordable and demonstrate real return if better working conditions are to become widespread. Disclosure of our supply chain is done in an effort to jump-start disclosure and collaboration throughout the industry and support efforts towards that final goal of market forces, providing the tipping point for the mainstreaming of best practice.





We believe that a strong corporate responsibility effort will be good for business. It helps us deliver value to our five core stakeholder groups: consumers, shareholders, business partners, employees and the community.

Second, we want to create innovative and sustainable products. We live to innovate – it's who we are. When our corporate responsibility initiatives begin leading us to new product development, it brings a new energy to our efforts. Whole divisions in our company open up to the prospects. Eyebrows are raised. There are results, already: We're finding ways to eliminate the toxic chemicals commonly used in making products and materials; teams are creating business models for generating revenue from ground-up old shoes; designers are developing products made of recycled polyester or organic cotton.

Third, we believe young people should have the right to sport and physical activity. For us, this is deeply intuitive. We see real value in physical fitness, and can see its direct impact on mental and physical health. We see value in competition and in teamwork; the lessons gained on fields of play, the ones gained alongside trusted teammates, apply at work. We see value in the hard physical work of those sports that require us to surprise ourselves with new sources of energy and stamina. Sport matters to us, for all sorts of reasons, not the least of which is pure joy. Our efforts to engage young people in sport and physical activity has pushed us in new directions, and has helped us see sport as a tool for positive social change. It can be a method of breaking down cultural barriers, or bringing people together on the proverbial level playing field.

We believe that a strong corporate responsibility effort will be good for business. It helps us deliver value to our five core stakeholder groups: consumers, shareholders, business partners, employees and the community. It will help us build our capacity to achieve supply chain excellence, deliver superior and innovative products, and deepen our relationship with consumers. It's why our sourcing managers are beginning to bring corporate responsibility data into their decisions about which factories merit an increase, or a decrease, in production orders; it's also why our corporate responsibility staff is spending time identifying future risks and opportunities for the company, and why they are calculating the return on our social and environmental investments. We understand that a well-managed company must reflect the society in which it operates, and it is through these social relationships that we will continue to evolve our efforts in years to come.

Phil Knight said it over five years ago: To be successful in business in the 21st century, you must successfully integrate corporate responsibility into the heart of the business. Doing this is a sometimes uncomfortable, frustrating adventure in the unknown. It is made painful when efforts are taken out of context and turned into news headlines. It is made worthwhile every time we see the positive impact our company and our employees have on a young person's life, or on workers in our supply chain. It is reinforced every time we see employees integrating corporate responsibility into their day-to-day work and coming up with innovative, appealing products that push the boundaries in both design and sustainability.

This is what drives us. We are in it for the long term. As everyone at Nike says so often, there is no finish line.

A handwritten signature in black ink, appearing to read 'Mark Parker'.

Mark Parker
Co-President

A handwritten signature in black ink, appearing to read 'Charlie Denson'.

Charlie Denson
Co-President



Reporting

SCOPE OF REPORT

This report focuses primarily on activities and data related to the Nike brand, which represents approximately 89% of our FY04 revenue. Except where noted, it does not cover information related to subsidiaries owned by Nike, Inc.: Cole Haan, Bauer Nike Hockey, Hurley International, Converse and Exeter Brands Group.

Our goal is to extend corporate responsibility (CR) activities and reporting to cover all Nike, Inc. subsidiaries; we do not, at this time, have a specific timetable for their integration into our reporting.

Timeframe

This report covers Nike's 2004 fiscal year (FY04), which began June 1, 2003 and ended May 31, 2004. Data covers FY04, unless otherwise noted. Because we did not issue external corporate responsibility reports for FY02 and FY03, some text refers to activities in those years. A small number of important events that took place after FY04 are covered here; their inclusion reflects the impact or influence the events may have on Nike's future direction in this area or requests from our Report Review Committee.

GRI Guidelines

In developing this report, we relied heavily on the guidelines issued by the Global Reporting Initiative (GRI). The GRI offers a comprehensive framework for reporting a company's impacts and activities. A GRI index, located at the back of this report, can help readers match this report with sections of the GRI. (For more information, see: <http://www.globalreporting.org>)

We strongly support the GRI as a core tool for CR reporting because it has credibility with a broad cross-section of stakeholder groups. We are committed to using the GRI Guidelines, and we support efforts to advance reporting on the basis of the GRI.

We are working actively with the GRI to create a working group to develop specific guidelines for the apparel and footwear industries. This initiative, set to begin in 2005, will involve a diverse group of stakeholders.

Ceres

Nike has been an endorsing member of Ceres since 2000. Ceres is a coalition of investment funds, environmental organizations and public interest groups. Ceres' mission is to move businesses, capital and markets to advance lasting prosperity by valuing the health of the planet and its people. The GRI emerged from Ceres.

Global Compact

Nike continues to support the United Nations Global Compact, having endorsed its principles at the inaugural meeting in July 2000.

The Global Compact is a voluntary international citizenship network involving the private sector and other social actors. Its goal is to advance responsible corporate citizenship as defined in its 10 principles covering human rights, labor rights, corruption and environmental responsibility. The Global Compact facilitates learning and dialogue around the key principles and provides a framework for transparency. The Global Compact index, located at the back of this document, can help readers match this report with the principles. (For more information, see: <http://www.unglobalcompact.org>)

This report describes actions we have taken to implement the Global Compact principles, and serves as our Communication of Progress as required for all companies that endorse the Global Compact principles.

Reasons for Reporting

Transparency is an essential element of our corporate responsibility strategy.

It is also expected practice for industry leaders. A 2004 study by the research institute, AccountAbility, found that 72 of the world's 100 highest revenue companies produced annual sustainability reports.¹

Nongovernmental organizations (NGOs), trade unions, students and academics, shareholders and others have taught us a great deal about how best to live up to our company values; we want to continue learning from them. By providing a clear explanation of how our business and industry work, our challenges and opportunities as we understand them, our strategic corporate responsibility goals and the progress we are making toward them, we can put these stakeholders in a position to offer relevant and thoughtful feedback.

We want to build trust and enable stakeholders to judge us not on perception, but fact. Transparency is an essential tool in this process.

Materiality

Recognizing that some issues are more relevant than others, we developed the following checklist to guide us in determining what topics to cover in this report.

- **Major impacts and issues:** Based on internal life cycle impact analyses.
- **Policies and commitments:** GRI Guidelines, Nike Code of Conduct.
- **Peer benchmark:** CR Reports of industry peers.
- **Internal business processes:** Information used to manage CR internally.
- **Stakeholder input:** Priority issues as communicated by our stakeholders through our Report Review Committee and 2004 Stakeholder Forum.

¹<http://www.accountability.org.uk/news/default.asp?id=111>

Inevitably, we may have missed topics important to select individuals; it was our intention to prioritize issues raised most frequently by our stakeholders. We intend to continue to use this materiality framework as a guide for reporting in future years.

Approach to Reporting

Our transparency efforts and our commitment to reporting are not limited to this document. We see value in different methods of reporting and communicating.

Disclosure

This report can be viewed as disclosure of our corporate responsibility impacts. Our intent is to share information in a systematic and standardized way on issues that are most relevant to our internal and external stakeholders. We have used the GRI as a guide for our reporting and we have tried to identify key indicators and clarify what the numbers mean. Ultimately, this format may allow for greater ease in gauging year-over-year progress. Our intended audiences for this report include members of the socially responsible investment (SRI) community, employees, academics, NGO and advocacy organization leaders and individuals with an in-depth knowledge of corporate responsibility.

One of the major challenges that we faced in preparing this report was bridging the gap between different stakeholder groups. Much of the information we are reporting is used to help us manage our corporate responsibility impacts and drive improvements throughout our operations. We struggled with ways to present this information in a format that would be accessible to external stakeholders, comparable to the type of disclosure undertaken by our peers, and reflective of how the information is used to manage change within our business. This tension remains, and we hope to address it through our participation in the GRI sector supplement working group and through direct stakeholder engagement around the future of reporting.



We want to build trust and enable stakeholders to judge us not on perception, but fact. Transparency is an essential tool in this process.

Activities and Examples

While some readers may seek disclosure, others may look for inspiration, and we see great value in descriptive accounts of this work. So much of this work is new, for Nike and for others, and sharing the challenges we face (as well as best practices) plays an important developmental role. With the few anecdotes and pilot projects described in this report, we do not intend to imply success. We will be using our website and regular electronic mailings to keep stakeholders informed about other activities that are not included in this report.
(See <http://www.nikeresponsibility.com>)

Legal Challenges to Reporting

This is our first corporate responsibility report in three years. After releasing a report based on our FY01 activities, our commitment to transparency was tempered by a lawsuit: *Kasky v. Nike*. The suit, which was granted review but not, in fact, reviewed by the U.S. Supreme Court, led to a broad definition of commercial speech by the California Supreme Court. While we continue to be concerned with the broad definition and the risk it creates under California law, we must balance those concerns with our commitment to transparency and our need to maintain credibility. The growing number of companies that have reported from our industry sector and our improved internal systems for collecting data also played a role in our decision to report.

For more information on the *Kasky* case, please go to:
<http://www.nikebiz.com/kasky>

Assurance and Verification

We view assurance as a process designed to enhance the credibility and relevance of our CR report to its intended audience. For Nike, the Report Review Committee (described below) is a first step in exploring the best assurance options – for us and for our stakeholders. We expect that the demand for assurance will grow and include stakeholder engagement as well as data and systems verification, but we are still in the early stages of developing this broader assurance strategy. One

thing we know is that standardized reporting mechanisms will help facilitate its development.

It was beyond the scope of the Report Review Committee to provide verification of the information contained in this report. At this time, we work with a variety of organizations to evaluate the quality of our systems or data in different areas of corporate responsibility. We do not yet have a comprehensive verification program in place, and hope to continue a dialogue with stakeholders about whether such a program should be a priority for Nike given the extensive investment that it would require. We plan to develop our strategy for long-term assurance and verification in FY06. In the meantime, the following list provides a sampling of the organizations that have provided us with independent assessments of our work:

- **Fair Labor Association:** Independent auditing of working conditions in contract factories
- **CH2M Hill:** Environmental data
- **Center for Energy and Climate Solutions:** Climate Savers
- **Program Environmental Resource Trust:** Greenhouse gas emissions
- **Centers for Disease Control and Prevention:** NikeGO - USA
- **Citizenship CSR Consultancy:** NikeGO – EMEA (Europe, Middle East and Africa.)

Feedback

We acknowledge that there is an ongoing debate about how best to present information on our social and environmental reporting and performance. We welcome your views on these topics. Please contact us at:

Corporate Responsibility
Nike, Inc.
One Bowerman Drive
Beaverton, Oregon 97005

Email: <http://responsibility@nike.com>
Take our online survey at:
<http://www.nikeresponsibility.com/reports>



REPORT REVIEW COMMITTEE

For advice in drafting this report, we asked for help from a Report Review Committee, made up of experts from the NGO, academic, trade union, investor and business communities. (These constituencies reflect the intended audience for this report.)

The group was chaired by Ceres. Committee members were identified by Ceres and AccountAbility, in consultation with Nike. Meetings were facilitated by SustainAbility. Advice on the use of the AA1000 Assurance Standard was provided by AccountAbility. (AccountAbility and SustainAbility are UK-based organizations focused on corporate social responsibility and sustainable development.)

The committee met for the first time in September 2004, during the initial planning stages for this report. Their feedback has helped in setting the scope, coverage and focus for this report, and will feed into our decision-making for reporting in future years.

The Committee met again in February 2005 to comment on a draft report and assess our response to their suggestions. You can read their feedback, unedited by Nike, on page 12.

The Report Review Committee members were:

— **Andrew Brengle**, Senior research analyst specializing in environmental issues, KLD Research & Analytics, Inc. KLD is the leading provider of social research for institutional investors.

— **Chris Tuppen**, Head of Sustainable Development and Corporate Accountability, BT.

— **Deb Hall**, Director of Accountability Programs, Ceres. Ceres is a coalition of investment funds, environmental organizations and public interest groups.

— **Liz Cook**, Director, Sustainable Enterprise Program, World Resources Institute (WRI). World Resources Institute is an independent nonprofit organization working to protect the Earth and improve people's lives.

— **Liz Umlas**, Senior research analyst specializing in human rights and labor issues, KLD Research & Analytics, Inc.

— **Maggie Burns**, Freelance consultant in the NGO field of Labor Rights.

— **Neal Kearney**, General Secretary, International Textile, Garment & Leather Workers Federation (ITGLWF). The ITGLWF is an International Trade Secretariat bringing together 217 affiliated organizations in 110 countries, with a combined membership of over 10 million workers.

— **Thomas N. Gladwin**, Max McGraw Professor of Sustainable Enterprise and Director of the Erb Environmental Management Institute, jointly in the Ross School of Business and School of Natural Resources and Environment at The University of Michigan.

— **Vidette Bullock-Mixon**, Director of Corporate Relations and Social Concerns, General Board of Pension and Health Benefits of the United Methodist Church.

*Liz Umlas replaced Andrew Brengle for the second meeting of the Report Review Committee.

*Members of the Report Review Committee participated in their individual capacities rather than as members of the organizations with which they are affiliated.

Report Review Committee Statement

BACKGROUND

Our Report Review Committee has varied expertise in labor, human rights, environmental, social, economic and diversity issues, and a common commitment to transparency and multi-stakeholder engagement. We also share an interest in supporting innovative efforts by corporations to address these challenging issues. Some came to the Committee with experience engaging with Nike; others were familiar with Nike through its reports, media, marketing and/or third-party analysis. We agreed to serve on the Committee as individuals rather than as representatives of our respective organizations.

We appreciate Nike's decision to resume corporate responsibility (CR) reporting after three years, and we have welcomed the opportunity to be part of Nike's process of multi-stakeholder engagement throughout its reporting process. Nike demonstrated its commitment to stakeholder engagement by actively engaging the Committee while the report was in development, making significant improvements after receiving the Committee's feedback on the draft version of the report, and publishing this unedited public statement in the finished report.

REPORT ASSESSMENT

Nike asked the committee to work with the AA1000 Assurance Standard* and provide an opinion on how well Nike's report:

(a) covers Nike's key business impacts and includes information on the issues of greatest concern to Nike's stakeholders (Materiality),

(b) indicates Nike's awareness of and ability to understand and address its impacts (Completeness), and

(c) provides evidence that the company engages and listens to its stakeholders (Responsiveness).

Our task was to look at various sources of information that could be used to evaluate Nike's performance, rather than comment on performance. The Committee would like to commend Nike's announcement in this report that it will disclose the names and locations of its supplier factory base. This is a groundbreaking step in transparency and should help remove barriers to the collaboration needed to improve labor standards throughout the global apparel and footwear industry.

* AA1000 is an open source Assurance Standard that covers principles applicable to a robust and credible assurance process and the essential elements of a public assurance statement. For more information, see <http://www.accountability.org.uk>

Our assessment of this report is as follows:

Materiality

(a) Nike's report covers the key impacts of the "Nike brand" business activities and appropriately places most emphasis on the labor and social impacts on workers in its supply chain. The report further describes how Nike is beginning to integrate corporate responsibility into its fundamental business practices, through incorporation of CR compliance, price, quality and delivery into the Balanced Scorecard used for its purchasing process. The environment section appropriately focuses on innovative and sustainable product design, manufacturing impacts, climate change and toxics elimination.

Completeness

(b) The report lacks consistent provision of multiple years of performance data for its key indicators, which would permit improved evaluation of impacts over time. Nike indicates in the report that this is one of its challenges and notes its intention to develop the improved metrics and management systems needed for better reporting in future years. While the report may seem to provide excessive information on Nike's process of setting up diagnostic and compliance tools and systems related to workers and factories, we feel that this information will be important for future reference.

Responsiveness

(c) The report documents Nike's progress since the last report in engaging varied stakeholders on issues and impacts, through efforts such as the Stakeholder Forum held in 2004, numerous stakeholder partnerships and the formation of this Report Review Committee. In response to stakeholder interest in seeing targets reported as well as past performance, Nike's report does contain some targets for future improvement, and indicates where it will be developing additional targets and more specific timelines for meeting these. Nike's decision to disclose the names and locations of its suppliers indicates a notable level of responsiveness to stakeholders concerned about labor practices.

The report's candor on the significant challenges of addressing labor standards within its global supply chain is welcome, and may facilitate discussion on

how to tackle these challenges. While noting that monitoring is not a sufficient or long-term solution to raising labor standards, the report presents Nike's extensive and evolving efforts to manage monitoring, integrate compliance into its business strategy through the Balanced Scorecard, and pursue multi-stakeholder initiatives that could lead to more systemic industry-wide improvements.

We commend Nike's use and support of the Global Reporting Initiative *Sustainability Reporting Guidelines* as the leading standardized framework for this type of non-financial disclosure.

Overall the report includes a useful set of major sections, presenting issues and impacts, strategy, business integration, multi-stakeholder partnerships and targets. It has also charted some new territory by reporting on its public policy positions.

Recommendations for Future Reporting

■ **Improve Information Systems.** Nike needs to implement an improved data collection and information management system in order to produce more robust and reliable data for future reports.

■ **Report Progress of CR Integration Into Business.** Future reports should address progress implementing the Balanced Scorecard, noting how buyers for Nike are managing the tension between CR compliance, price, quality and delivery goals.

■ **Expand Coverage of Subsidiaries' Performance.** The Committee commends Nike's stated plans for more comprehensive disclosure and urges reporting on the timelines and progress for integrating each subsidiary's performance in the next report, even if fully integrated data is not yet available.

■ **Continue to Report on Supplier Performance.** Disclosure of the supply base is a positive step for the industry, and future reports should note both the quantitative performance results of suppliers and their progress in establishing effective industrial relations. More detailed information on the training and education of the managers and workers at supplier factories is needed.

■ **Address Verification and Assurance.** We encourage Nike to produce a roadmap explaining how it will develop its assurance processes both internally and externally, and cover data verification as well as stakeholder engagement.

■ **Expand Coverage of Stakeholder Engagement.** While Nike's current report documents extensive stakeholder engagement and demonstrates how its partnerships and collaborations have benefited Nike, future reports would benefit from coverage of how Nike engages some of its keenest critics.

■ **Discuss Consumer Issues.** We agree with Nike that customers are a significant stakeholder group, and request that future reports address consumer-oriented issues, such as sports marketing, athlete sponsorship and sustainable consumption.

We recognize Nike for this candid and comprehensive report, and appreciated the opportunity to collaborate on this Report Review Committee. We recommend this type of process to other companies.

Submitted by:

Nike Report Review Committee

CORPORATE RESPONSIBILITY REPORT: PART II

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Corporate Responsibility Report

NIKE, INC. AND WHOLLY OWNED SUBSIDIARIES

Nike, Inc. is the world's leading designer, marketer and distributor of authentic athletic footwear, apparel, equipment and accessories for a wide variety of sports and fitness activities. Virtually all Nike products are manufactured by independent contract manufacturers, many of whom produce for other globally recognized brands. Most Nike products are made outside the United States.

Nike, Inc. includes the following wholly owned subsidiaries, based in the United States:

- Cole Haan Holdings, Inc., based in Maine, sells dress and casual footwear and accessories for men and women under the brand names of Cole Haan, g Series, and Bragano.
- Bauer Nike Hockey, based in New Hampshire, manufactures and distributes hockey ice skates, apparel and equipment, as well as equipment for in-line skating, and street and roller hockey.
- Hurley International LLC, based in California, designs and distributes a line of action sports apparel for surfing, skateboarding and snowboarding, and youth lifestyle apparel and footwear.

- Nike IHM, Inc., based in Oregon, makes AIR-SOLE cushioning components used in Nike footwear products and sells small amounts of various plastic products to other manufacturers.
- Converse Inc., based in Massachusetts, designs and distributes athletic and casual footwear, apparel, and accessories.
- Exeter Brands Group LLC, based in New York, includes the Starter, Team Starter, and Asphalt brand names and is the master licensee of the Shaq and Dunkman brands. The Exeter Brands Group is devoted to designing and marketing athletic footwear and apparel for the value retail channel. (The creation of Exeter Brands Group took place in FY05, but because of its significance, we chose to include it in this report.)

FINANCIAL PERFORMANCE

For complete information about Nike's financial performance, see our Form 10-K available on our website. Selected data for the company, including wholly owned subsidiaries, are shown here.

COMPANY PROFILE

Net Revenue by Global Region (millions)

	FY04	FY03	FY02
United States	\$ 4,793.7	\$ 4,658.4	\$4,669.6
EMEA	3,834.4	3,241.7	2,696.5
Asia Pacific	1,613.4	1,349.2	1,134.9
Americas	624.8	527.0	568.1
Other	1,386.8	920.7	823.9
Total	\$12,253.1	\$10,697.0	\$9,893.0



*Source: Datamonitor

Pre-Tax Income (millions)

	FY04	FY03	FY02
United States	\$1,015.1	\$ 963.2	\$ 956.0
EMEA	750.7	532.0	422.4
Asia Pacific	354.9	292.6	216.2
Americas	101.9	96.5	92.1
Other	75.3	5.2	43.7
Corporate	(847.9)	(766.5)	(713.1)
Total	\$1,450.0	\$1,123.0	\$1,017.3

Net Income (millions)

	FY04	FY03	FY02
Net Income	\$945.6	\$474.0	\$663.3

Net Revenues by Product Line (millions)

	FY04	FY03	FY02
Footwear	\$ 6,569.9	\$ 5,983.4	\$5,676.6
Apparel	3,545.4	3,130.0	2,801.3
Equipment	751.0	662.9	591.2
Other	1,386.8	920.7	823.9
Total	\$12,253.1	\$10,697.0	\$9,893.0

Global Sales Balance (percentage of sales)

	FY04	FY03	FY02
U.S. Sales	47%	49%	53%
International	53%	51%	47%

In the United States, we sell to approximately 28,000 retail accounts. During fiscal year 2004 (FY04), our three largest customers accounted for approximately 23 percent of total sales in the United States.

Outside the United States, we sell our products in over 120 countries through retail accounts, independent distributors, licensees, subsidiaries and branch offices. We estimate that we sell to more than 23,000 retail accounts outside the United States, excluding sales by independent distributors and licensees. Nike's three largest customers outside of the United States accounted for approximately 13 percent of non-U.S. sales.

Properties

See our website and Form 10-K for information about Nike offices and Nike-owned and operated facilities.

Employees

Nike, Inc. had close to 24,000 employees as of May 31, 2004. A small number of our employees at Bauer Nike Hockey, Inc. and in Europe are represented by a union. Nike, Inc. companies have never had a material interruption of operations due to labor disagreements.

	Employees
United States	11,970
Americas	1,076
Asia/Pacific	3,282
Europe, Middle East, Africa	6,075
Subsidiaries	1,888
Total	24,291



Taxes Paid (millions)

	FY04	FY03	FY02
CURRENT:			
U.S. Federal	\$185.3	\$125.6	\$156.5
U.S. State	43.3	33.6	32.0
Foreign	266.8	190.0	147.7
Subtotal	495.4	349.2	336.2
DEFERRED:			
U.S. Federal	3.9	11.3	(3.3)
U.S. State	2.4	8.6	3.3
Foreign	2.7	13.8	12.8
Subtotal	9.0	33.7	12.8
	\$504.4	\$382.9	\$349.0

According to a recent study by ECONorthwest, a Portland-based consulting firm, tax payments by Nike and its full- and part-time employees in FY04 paid approximately \$84 million to the State of Oregon, local governments and school districts. For the complete ECONorthwest study on Nike's economic impact in Oregon visit our website at <http://www.nikeinoregon.com>.

Contract Factories

Virtually all Nike brand products are manufactured by independent contract factories. The contract factory supply chain for Nike brand products involves over 800 factories. Factories move in and out of our source base as orders flow from Nike, which in part reflects changing consumer tastes and fashion trends. Any factory that has not received orders for more than 12 months is unauthorized and must obtain a new approval to receive additional production orders. For more information on the approval process, please see the *Workers in Contract Factories* section of this report.

COMPANY PROFILE

Nike Brand Approved Factory Base

	Apparel	Equipment	Footwear	Total
Americas*	102	26	9	137
EMEA	87	14	3	104
N. Asia	132	92	28	252
S. Asia	176	37	25	238
Active Total	497	169	65	731
Inactives	79	15	5	99
Total	576	184	70	830

Data as of May 31, 2004

*Includes the United States

Although the profile of the workforce varies by country, the majority of the more than 650,000 workers in Nike contract factories are women between the ages of 19 and 25 years old. For many workers, these entry-level, low-skill jobs may be their introduction into the formal workforce in emerging economies.

Nike Brand Contracted Factory Employee Count

	Apparel	Equipment	Footwear	Total
Americas*	36,364	6,077	2,127	44,568
EMEA	24,443	3,236	1,563	29,242
N. Asia	100,060	32,750	152,753	285,563
S. Asia	155,662	21,304	88,292	265,258
Active Total	316,529	63,367	244,735	624,631

Data as of May 31, 2004

*Includes the United States

All data is for Nike brand contract factories, including those producing products through agents and licensees and locally manufactured products for Nike country operations, for FY04 ending May 31, 2004, unless otherwise noted. Data do not reflect factories producing for Nike Inc. subsidiaries, except where those are factories shared with Nike brand orders.

Contract Factory Disclosure

Since the fall of 2000, as an independent decision to respond to college requests, we have publicly disclosed the names and locations of the approximately 100 contract factories involved each year in the production of collegiate licensed apparel. We were the first to do so.

Each year, we confidentially provide the full set of our contract factories making Nike-branded products to the Fair Labor Association (FLA), so that they may make appropriate, independent choices about which facilities they choose to audit.

Effective with this report, Nike is the first company in our industry to expand transparency by publishing online the names and addresses of all factories making Nike branded product. The list will include all Nike brand factories currently approved for production, including those that are active or inactive as of March 2005. This list can be found at <http://www.nikeresponsibility.com>. We aim to update the list on an annual basis as part of our Corporate Responsibility (CR) reporting cycle.

Nike was founded on a handshake. Implicit in that act was the determination that we would build our business based on trust, teamwork, honesty and mutual respect.

As we have grown from a two-man partnership to a global business, our task has been to maintain this same ethic across our operations. We have put in place corporate governance policies and practices to help us achieve this. In recent years, we have extended these to include corporate responsibility issues as a central part of our governance system.

Board of Directors

Nike's board of directors is responsible for corporate governance in compliance with the U.S. Sarbanes-Oxley Act and other laws, and the interests of our shareholders.

The board is currently composed of 10 members, eight of whom are independent non-executive directors as defined under the listing standards of the New York Stock Exchange. Six board committees share responsibility for overseeing specific policies and procedures, including audit, compensation, corporate responsibility, executive, finance and nominating and corporate governance.

Our Codes and Policies

Our code of ethics, *Inside the Lines*, defines the standards of conduct we expect of employees. The subjects it covers include the following:

- Equal opportunity
- Harassment and zero tolerance
- Environment, safety and health
- Sales agents, consultants and professional services
- Social responsibility
- Team equipment (Nike product)
- Product safety
- Export and import laws
- Protection of Nike information, ideas and intellectual property

CORPORATE GOVERNANCE

- Accurate records and reports
- Safeguarding assets and records
- Computing and information resources
- Fraud and theft
- Gifts and gratuities
- Conflict of interest
- Insider trading
- Antitrust and competition
- Compliance with laws and fair dealing
- Political contributions
- Sportsmanship
- No retaliation
- Performance violations

Every year, all employees are required to verify that they have read and understand *Inside the Lines*.

For more information on *Inside the Lines*, please visit our website at <http://www.nikeresponsibility.com/codeofethics>.

We operate a global toll-free *Alertline* for employees to confidentially report any suspected violations of the law or our code of ethics. Any reported concerns around accounting, auditing or internal control are communicated to the audit committee of the board.

We expect our suppliers to share our standards and to operate in a legal and ethical manner. While *Inside the Lines* covers the behavior of Nike employees, our Nike Code of Conduct covers contractors who manufacture Nike-branded products. It directs them to respect the rights of their employees, and to provide them with a safe and healthy work environment.

For a copy of our Code of Conduct for contract factories, please visit our website at <http://www.nikeresponsibility.com/codeofconduct>.

CR Management at the Board Level

One of the six committees on our board of directors is the corporate responsibility committee. Its members, as of May 31, 2004, include the following:

- Jill Ker Conway, non-executive director, committee chair
- Douglas G. Houser, non-executive director
- Jeanne P. Jackson, non-executive director
- John R. Thompson, Jr., non-executive director

The CR committee was established in 2001 to review significant policies and activities and make recommendations to the board of directors regarding labor and environmental practices, community affairs, charitable and foundation activities, diversity and equal opportunity, and environmental and sustainability initiatives. Nike's executive team attends the committee meetings.

The committee met four times in FY04 and reviewed strategies and plans for issues including:

- Communications and global issues management
- CR investments
- CR reporting and metrics
- CR strategic plan
- Diversity
- Environment, safety and health
- Establishment of a CR Business Leadership Team
- Evolution of our compliance programs
- Factory exit response plan
- MIT research collaboration
- Multi-Fiber Arrangement (MFA)
- Nike Foundation
- Stakeholder Forum
- Subsidiaries
- Value channel

CR Management at the Executive Level

In FY04, we established the CR Business Leadership Team. They set policies and oversee the work of our CR team and departments responsible for managing CR issues on a day-to-day basis.

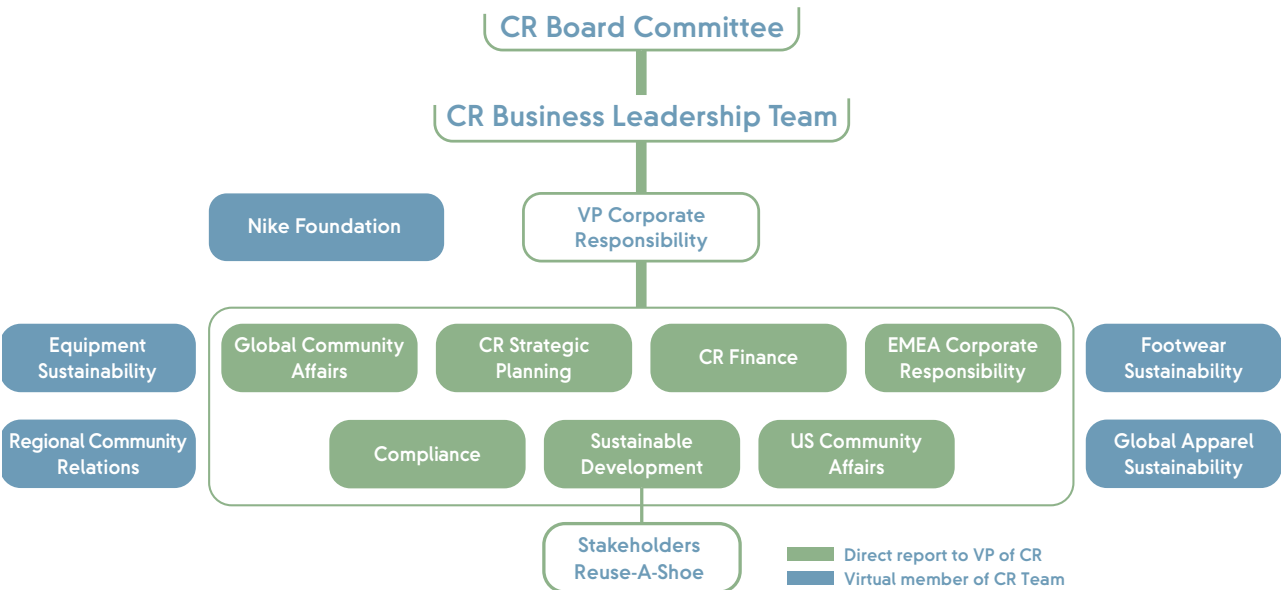
Business Leadership Team members during FY04 include the following:

- Co-Presidents, Nike Brand
- VP, Corporate Responsibility
- VP, Global Apparel Operations
- VP, Subsidiaries and New Business Development
- VP and General Counsel
- VP, Global Equipment
- VP, Global Footwear
- VP, Corporate Communications
- Director, Global Apparel Operations and Corporate Responsibility

Responsibilities of the Business Leadership Team include the following:

- Assisting in developing overall CR policies and strategies
- Reviewing and approving policies and strategies prior to board approval
- Reviewing and approving overall CR investments, divestments and reinvestments
- Reviewing and monitoring progress against overall CR objectives and plans and helping promote/direct achievement of those objectives
- Reviewing and approving global, regional and country CR organizational structure and accountabilities
- Helping promote further integration of CR into the business through active advocacy for CR, both internally and externally

Corporate Responsibility Organization



*Some of the positions have dual reports to other departments and regions.

CORPORATE GOVERNANCE

Integration of Corporate Responsibility at the Operational Level

Corporate responsibility encompasses a broad range of subjects and requires a broad range of skills. At the operational level, it is managed by full-time CR employees and other relevant departments. These include labor and environment, safety and health compliance (ESH); community affairs, corporate communications, government affairs, legal, human resources and diversity; reporting, stakeholder engagement, environmental initiatives, strategy development and product sustainability.

As of December 2004, nearly 150 Nike employees work on CR issues as their primary function or have CR work as a significant portion of their workload.

Leadership Changes

In October 2004, Hannah Jones, former director of Corporate Responsibility in Europe, Middle East and Africa (EMEA), became vice president of Corporate Responsibility. She will serve as a representative to the Nike Corporate Responsibility Business Leadership Team and our board of directors' corporate responsibility committee.

Hannah will focus on integration, making corporate responsibility the job of every employee at Nike and incorporating it into strategic plans throughout the business.

Maria Eitel, our first vice president of Corporate Responsibility, became President of the Nike Foundation. After seven critical years of helping build our CR strategy and programs, she will focus the work of the Nike Foundation on addressing poverty alleviation and gender inequality.

MANAGEMENT DISCUSSION & STRATEGY

COMPANY STRATEGY AND CORPORATE RESPONSIBILITY

Nike's overall corporate strategy focuses on delivering value to shareholders, consumers, suppliers, employees and the community. We can achieve this by continuing to focus on our mission: To bring inspiration and innovation to every athlete in the world. And according to Nike co-founder Bill Bowerman, if you have a body, you are an athlete.

To this end, we as a company have been building our capability to

- Deepen our relationship with consumers
- Deliver superior, innovative products to the marketplace
- Make our supply chain a competitive advantage, through discipline and excellence
- Accelerate growth through focused execution

In each case, we see that corporate responsibility dovetails with these larger corporate goals:

- Building trust around our corporate responsibility initiatives can increase loyalty among existing customers, rebuild trust with old ones, and introduce us to new communities.
- As noted in the *Environment* section of this report, our focus on sustainable product innovation is slowly becoming evident on retail shelves. Over time, we'll consider how we engage customers about the new value embedded in these products.
- Understanding the complexities of environmental and social issues is key to supply chain excellence.

The *Workers in Contract Factories* section of this report will show that we are gaining a better understanding of the issues we face in this arena.

Although we have seen progress over the years, there is still need for improvement. And we will only see significant improvements within the global apparel and footwear industry when market forces reward corporate responsibility and good working conditions are seen as a key indicator of manufacturing excellence.

- Focused execution is best achieved not in isolated pockets, but across the board. We believe we will improve other business systems by improving our systems in corporate responsibility. And, although not proven, a strong corporate responsibility program is an indicator of strong overall corporate management.

Corporate Responsibility Strategy

As we work to support Nike's overall corporate strategy, our approach to corporate responsibility follows a set of clearly identified steps:

- Understand **issues and impacts**
- Set long-term **strategy** and targets
- Drive **business integration** and align incentives
- Drive industry change through **multi-stakeholder partnerships**
- Measure **performance**

Management Discussion & Strategy

We have attempted to structure this report – specifically the sections on *Workers in Contract Factories, Employees and Diversity, Environment and Community* – to demonstrate what we have done within each of these steps.

Understand Issues and Impacts

We start with the work of understanding our issues and impacts. This helps us focus and prioritize our efforts. Not only are we finding that this process is best undertaken with rigor, but we're also discovering it is best undertaken in consultation with others, because both internal and external stakeholders help us gain new insights and understand the perspectives of others.

Discussion of impact leads to understanding which strategies and tools will bring about positive change. It involves analysis of root causes and an in-depth understanding of business models. It demands that we engage with government, civil society and other businesses already active in the arena to benefit from their understanding of the issues and impacts. It calls on us to be inventive, innovative and to challenge our assumptions.

It is the first step in an iterative process as our issues and impacts – and our understanding of them – evolve. This notion of constant change sets the tone for the remaining steps.

In performing our self-assessment across the breadth of corporate responsibility efforts, we have gained a fuller understanding of our impacts and the issues we face as a business.

We also recognize that we need to do more work to understand the overall global corporate responsibility impacts of our business. Research is frequently regional or product specific, and no centralized mechanism for sharing this information currently exists.

Set Long-Term Corporate Responsibility Goals

Based on our understanding of our issues and impacts, we set three goals that reflect where we believe we can have the greatest effect on our business and on the world around us.

Our three corporate responsibility goals include the following:

- To effect positive, systemic change in working conditions within the footwear, apparel and equipment industries
- To create innovative and sustainable products
- To use sport as a tool for positive social change, and campaigning to turn sport and physical activity into a fundamental right for every young person.

These are long-term aspirations. Putting them in writing should not suggest we're close to accomplishing them; it instead shows how far we must travel.

Over the past decade we have primarily focused on compliance-related issues, and often in a state of continuous crisis. In regards to the environment and community, innovations have continued to emerge from across the company, but often without the benefit of a comprehensive and coordinated plan. Therefore setting focused, strategic goals is new to our team as well as a key challenge for us going forward.

In setting three corporate responsibility goals for the company, we know we must focus even if that means letting go of good programs currently in existence.

Drive Business Integration and Align Incentives

Within Nike, work often unfolds in silos – with business units sharing information vertically within their unit, but not horizontally across the company. Social and environmental expertise is often confined within our corporate responsibility team. In the past, a degree of separation has existed between CR and the rest of the company.

While product teams are aware of our corporate responsibility goals and support them, their performance is judged in ways that have little to do with corporate responsibility. For example, if a product team misses cost estimates, they hear about it from managers who want to know why it happened or what can be learned from the experience. If the same product team selects factories with low compliance scores, our CR team would hear about it, but the business unit might not be aware of the problem.

The steps we're taking to change this are a central component to our long-term strategy for FY05 and beyond. We will focus on integrating CR into strategic plans and building accountability for our CR objectives.

Drive Multi-Stakeholder Partnerships and Industry Change

From our early years up to the 1990s, the stakeholders we thought most about were athletes and consumers. In the 1990s, we ignored an emerging group of stakeholders. We learned a hard lesson.

Today, engagement with stakeholders (anyone affected by, or affecting, our business operations) is increasingly important to Nike. They help us to prioritize key issues and develop and implement our CR policies. We've learned a great deal from this interaction. Non-governmental organizations (NGOs), trade unions and others have opened our eyes to new issues and viewpoints, and have enabled us to draw on their experience and expertise. This does not mean that we will always agree with our stakeholders, but we know from experience that constructive engagement is usually the approach that brings about the best insight to the challenges we all have an interest in addressing.

But consultation with stakeholders is only part of the value of engagement. The industry is at a crossroads, and individual companies are limited in what they can achieve acting independently.

Nike may be a prominent brand, but we account for under two percent of the global \$800 billion footwear and apparel industry. We contract with factories employing an estimated 650,000 workers, compared to an estimated 50 million workers worldwide. Because we're the number one footwear brand, we sit at the top of the industry pyramid, working with the top suppliers. So the issues we see in our contract factories are not only indicative of greater issues across the industry, but, given our rigorous screening process, we suspect the issues are more pervasive.

That is why we believe disclosing our contract manufacturing base has the potential to open the door to a deeper level of collaboration with our stakeholders in addressing our industry's most material issue – working conditions in manufacturing facilities.

Even though we're working hard with our suppliers and looking back into our own business processes to create mechanisms that enable corporate responsibility, it's only when market forces enable corporate responsibility that widespread change will occur.

So what could happen in a world where supplier data is openly shared?

This disclosure should enable brands to share information about compliance performance and minimize duplication of efforts. Lowering the price of entry into corporate responsibility means that more can and must join and commit.

Management Discussion & Strategy

In turn, monitoring becomes a less cumbersome process for suppliers. There is also an increased incentive to be proactive, which allows those suppliers investing in corporate responsibility to use it as a part of their proposition to other buyers. Monitoring also becomes optimized allowing brands to shift resources to capacity building.

All of this should support efforts to move to common standards, greater collaboration and greater transparency, which in turn supports the development of a marketplace where responsibility and competitiveness go hand-in-hand.

Measure Performance

For each goal, we plan to establish targets and timelines to gauge progress. Some of these are noted in subsequent sections of this report and others we are still in the process of defining.

This is an area where a great deal more work is needed. As a globally dispersed team, it has been difficult to set global targets, and even harder to measure performance against them. You will find that targets and concrete measurements of performance are missing; developing these are a key objective for our team in FY05 and FY06.

Because data is usually quantifiable and comparable, measuring performance for much of our environmental work is relatively straightforward, but demonstrating measurable performance for working conditions within our contract factories is more difficult. We do not feel that audit results are a useful measure of progress, but a broad indicator of where problems lie. We have evidence of success in pockets, but without comparative measures over a series of years, it

remains anecdotal. Identifying the appropriate metrics and tracking progress will be a major task for the years to come, which we plan to pursue through multi-stakeholder initiatives, including the Global Reporting Initiative (GRI) reporting sector supplement initiative.

With our community investments, measurement is also challenging. For most of the programs we support, we tend to track the number of grants, programs or dollars, but these metrics don't answer the key question: Did they have an impact on a young person's life? For some of our projects, including those covering NikeGO in the United States and our programs in the EMEA region, we have pioneered impact assessment methodologies. For our other community affairs programs, the goal is to shift from measuring how much we give to measuring the real impact of the investments.

We realize that while we have a great deal of information to report, we still need to identify key indicators that we will use to set interim and medium-term targets for measuring our performance.

We will be seeking out others to join us in disclosing supply chains, and engaging with trade unions, civil society and government bodies to consider how disclosure can unlock collaboration.

So while we have much work to do internally to address our corporate responsibility challenges, we do not believe Nike has the power to single-handedly solve the issues at stake. This will only come through working with others in the industry through a variety of multi-stakeholder partnerships. And this is true for all areas of corporate responsibility, from compliance and environment to community investment programs.

Stakeholder Engagement

Nike's direct stakeholders include consumers, employees, investors, governments, retailers, athletes and athletic associations, suppliers and workers in our supply chain. Indirect stakeholders include academics, the media, trade unions and NGOs.

In addition, we have relationships with a large number of external groups. In order to have effective, quality engagements, we must prioritize and become more selective about groups with whom we will engage. For this reason, we focus on stakeholders with some of the following characteristics:

- **Legitimacy:** They have a direct stake in an issue, or there is a general public perception that they should be at the table.
- **Networked:** They are part of extensive networks and can bring perspectives from large numbers of stakeholders around a particular issue or within a particular region.
- **Expertise, resources and capabilities:** They have specific knowledge, resources or capabilities that can help us understand and address corporate responsibility challenges and opportunities.
- **Willingness to engage constructively.**

Approaches to Engagement

Different stakeholders require different engagement methods. We take a portfolio approach to stakeholder engagement with multiple approaches and varied levels of investment. This approach enables us to reach a larger number of stakeholders, investing more deeply with those that are more directly linked to our business. Examples of our stakeholder partners are listed throughout this report. The different forms of engagement include:

Report/Inform	Consult/Involve	Support	Multi-Stakeholder Partnerships
Provide information for stakeholders in a range of ways to update them on our progress (e.g., CR Report, website, e-newsletters, participation in socially responsible investor [SRI] surveys).	Seek input and guidance from external stakeholders to understand diverse perspectives (e.g., stakeholder forums, informal one-on-one meetings, surveys, etc.).	Provide support in the form of endorsements (e.g., for the GRI or Global Compact principles) or practical/philanthropic (e.g., community activities and programs).	Participate in coalitions, partnerships, projects, etc. for leverage purposes (many can usually accomplish more than one) or to access the knowledge, resources and experience needed to tackle issues effectively.

For a discussion of the challenges we have identified through stakeholder engagement, see the *Challenges and Opportunities* section of this report.

Management Discussion & Strategy

LEARNING FROM STAKEHOLDERS: NIKE'S FY04 STAKEHOLDER FORUM

We held our first global Stakeholder Forum in February 2004. Approximately 70 people took part in this two-day event, including 30 Nike employees and representatives from environmental and worker rights NGOs, trade unions, investors and suppliers. We could not include all of our stakeholders, but tried to include a diverse, representative group. Stakeholders were invited on the basis of their history of constructive engagement with Nike or their expertise on a particular topic. While the forum allowed for a broad discussion of Nike's CR strategy and goals, we also focused in-depth discussion around key emerging issues (China, women in the supply chain and MFA) that might best be addressed through a multi-stakeholder network approach.

Participants were asked for their views on our CR plan and to identify what they regard as the most important CR issues for Nike. Their feedback emphasized the following:

- CR issues must be integrated into Nike's core business strategies, with transparency on how this is being done. Participants also wanted to see more specific and measurable CR goals, particularly on social issues.
- Labor issues are an important priority for Nike's CR program and an area where stakeholders would like more information. Stakeholders recognized that Nike had made a good start at addressing labor practices in contract factories but wanted to see further progress. They identified freedom of association as a key issue, expressing concern about the challenge of adequate worker representation in countries such as China. They also identified phase-out of the Multi-Fiber Arrangement (MFA) as a key issue.
- Many participants highlighted support of women and girls in developing countries as a good opportunity for Nike to help bring about positive change. This included advocacy of women's rights on issues such as education and maternity leave, and a particular focus on the unique needs of adolescent girls.
- Environmental discussions focused on the specific challenges of China, types of materials used in Nike products, and concerns about water scarcity. There was positive feedback on Nike's goal of waste and toxics elimination.

Feedback from the forum is helping us prioritize our CR efforts. For example, the discussion led to the formation of the Multi-Fiber Arrangement forum (MFA forum), a multi-stakeholder group looking at ways to further understand and explore options to ease the impacts of MFA phase-out on workers and communities. (See *Challenges and Opportunities* section.)

Responsiveness

We are working on developing systems to enhance Nike's responsiveness to stakeholders with whom we are actively engaged. To this end, SustainAbility, a UK-based research, advocacy and consultancy company, completed an assessment of all the feedback we have received from stakeholders in the past several years. To read this assessment, please see our website at <http://www.nikeresponsibility.com/reports>.

We intend to continue seeking direct feedback from stakeholders, but we are exploring ways this might be achieved through existing networks or in conjunction with other companies to reduce the burden on stakeholders and ourselves.

Nike's approach to labor conditions in our contract factories is evolving.

We've evolved from a focus on our own Code of Conduct to advocating common standards across the industry. We've evolved from outsourcing labor monitoring to relying on a trained team of internal monitors and support for common monitoring platforms such as the Fair Labor Association. We are evolving from a focus on monitoring to a focus on capacity building. We are evolving from an exclusive focus on factory floor impact to an exploration of ways to help change the industry through transparency and multi-stakeholder collaborations.

These changes are driven by awareness that structural issues endemic to the global footwear, apparel and equipment industries affect an individual company's ability to change conditions in any particular factory.

This awareness is due to our monitoring processes, providing us with clearer data on issues; our analysis of root causes of non-compliance; and active listening and engagement in the broader dialogue with civil society, institutions and businesses around supply chain working conditions.

Since our last public report in 2001, we have focused on refining our skills at (a) identifying risk of code compliance; (b) uncovering issues; and (c) implementing strategies that can be used to drive performance and enable change within Nike internally and on a broader level.

We have become more systematic in identifying non-compliance risk, and we have become increasingly adept at uncovering issues. But despite anecdotal

instances of success, we remain profoundly challenged to understand how to systematically measure the impact of our own interventions. We are also challenged by how we play a role in enabling widespread change within the industry, which we now know is critical to facilitating change within our contract supply chain.

Our first step in responding to this challenge is to disclose our contract factory base. We believe this will pave the way for other companies to do the same, and this disclosure could be the key to unlocking collaboration necessary to create sustainable change.

Transparency should encourage factories to use corporate responsibility as a point of differentiation and to be rewarded by brands that are proactively seeking responsible factories. Transparency should also increase the incentive of brands to work with factories that demonstrate CR excellence.

WORKERS IN CONTRACT FACTORIES

If taken up by other companies, disclosure should provide a clear roadmap for collaboration in the form of coordinated monitoring and remediation at shared factories. This will allow us to devote more resources to fixing problems rather than just uncovering them. Most importantly, all of these steps should lead to greater improvements in working conditions than what we could achieve alone.

While we cannot say with absolute certainty what greater levels of factory disclosure will unleash, we know that the current system has to be fundamentally transformed to create sustainable change.

Scope

Our contract supply chain is continually changing. In FY04, Nike placed orders in 122 new factories and discontinued orders at a total of 34 factories; these decisions were based, in part, on shifts in consumer demand and trends. Other reasons that orders were shifted relate to the performance of that factory with respect to quality, delivery, price and corporate responsibility.

Currently, Nike's full compliance program covers contract factories manufacturing Nike and Jordan branded products. Cole Haan and Bauer Nike Hockey brands are covered by shared compliance efforts between Nike and those brands. At the close of FY04, Hurley, Converse and Exeter Brands were not yet in our system.

Unless otherwise noted, this section of the report includes information on contract factories producing Nike and Jordan branded finished products through our global manufacturing group, as well as through agents and licensees for FY03 and FY04, ending May 31, 2004. The data does not reflect factories producing for Nike, Inc. subsidiaries, except where those factories produce for the Nike brand. We do not currently have a timeline or a model for the extension of our compliance standards – labor and environment, safety

and health – to our subsidiaries, but it is an issue that we are actively discussing internally.

Codes and Standards

Our Code of Conduct for labor practices – adopted in 1992 and regularly evaluated and updated – outlines our expectations for contract factories around labor and environment, safety and health.

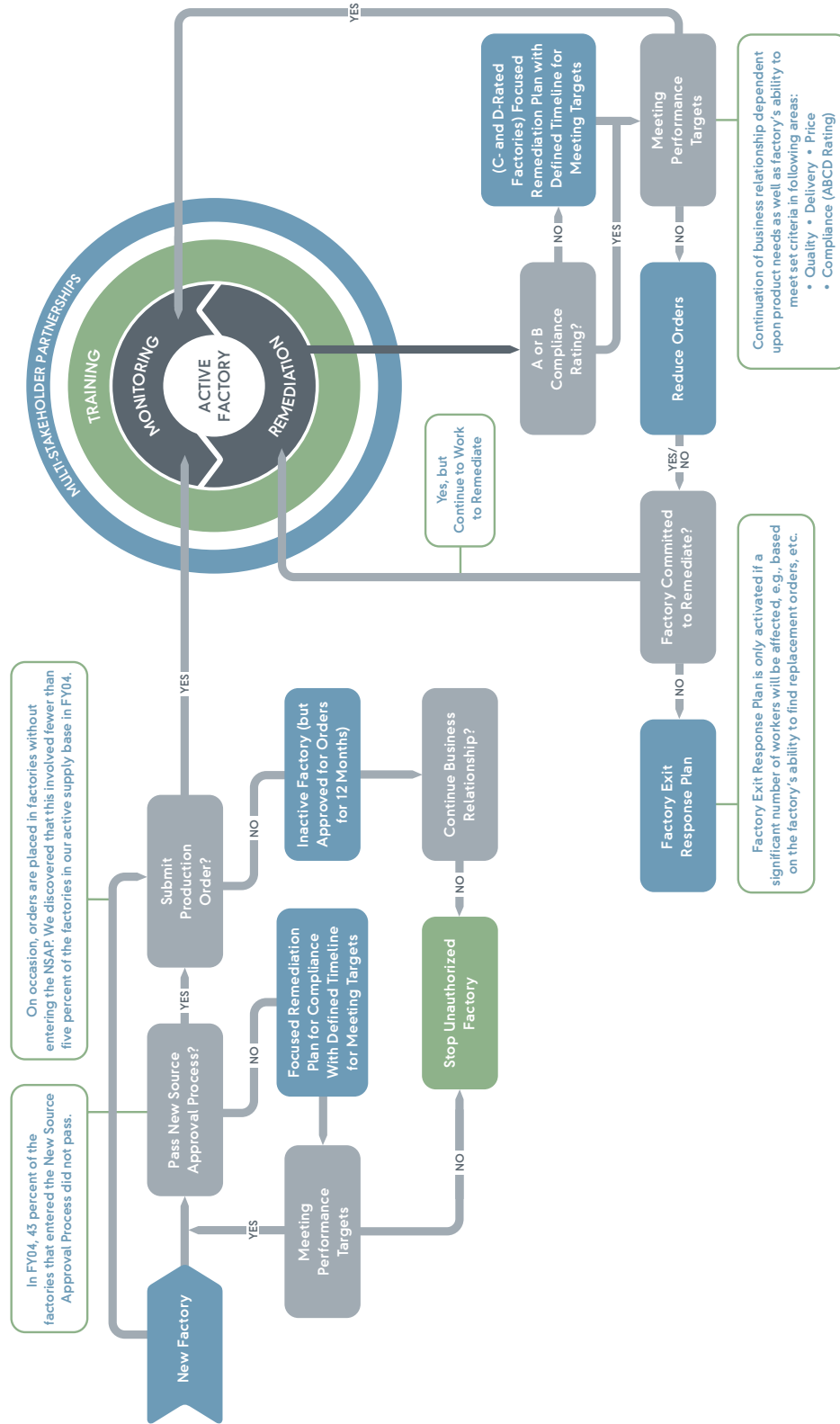
The code is a set of broad principles derived from fundamental International Labor Organization (ILO) conventions, universal principles of human rights and other relevant standards. Factories are directed to display the code, in languages spoken by their workers, and to provide training on the code to their workers. Our Code of Conduct requires compliance with local laws if local standards exceed our own. The broad principles of our Code of Conduct are expanded upon in our Code Leadership Standards (CLS), which cover 13 standards for management of people, nine for management of environmental impacts, 23 for safety and six for health – a total of 51 standards. (Nike's Code of Conduct is available on our website at <http://www.nikeresponsibility.com/codeofconduct>.)

STRATEGY

Our approach is based on

1. Discovering and understanding issues through monitoring and audits
2. Addressing our impacts through the following focus areas:
 - a. **Business integration** and the alignment of purchasing with our compliance standards
 - b. **Building the capacity of our contract factories** to make change through training and assisting with remediation
 - c. Working through **multi-stakeholder partnerships** to address issues endemic to our industry and to leverage resources and expertise that we may not have internally

Compliance Life Cycle



WORKERS IN CONTRACT FACTORIES

Factory Compliance Life Cycle

One way to understand our compliance programs for contract factories is to use the analogy of a life cycle.

At the beginning stage, we follow a six-step New Source Approval Process (NSAP) to select factories. Once a factory is approved and begins active production for Nike, the compliance team focuses on monitoring and assisting factory remediation of compliance issues that inevitably arise. Factories with whom we have longer-term relations may also benefit from Nike-supported training and other forms of capacity building to help the factory develop its own CR management capabilities.

When business circumstances change and we end our orders with a factory, we may also apply a factory exit process. Like the New Source Approval Process, the exit process has a series of defined steps. And it is usually applied only when our exit from a factory could create significant dislocations for the workforce.

It is within the context of this life cycle that our strategy – focused on business integration and multi-stakeholder initiatives – is implemented.

Stage One: New Source Approval Process

A multi-step process is required when a Nike business unit seeks to add a new factory to the source base.

The steps include the following:

- Factory profile
- Inspections for quality
- Environment, safety and health and labor inspection (SHAPE – described below)
- Third-party labor audit
- A review of the need for a new factory
- Approval by the compliance department

The process is intended to weed out unnecessary additions to the supply chain, or factories that do not have CR performance at a sufficient level. In FY04, 57 percent of factories that had the basic inspections performed were approved for production. The disapproval rate of 43 percent, and the fact that almost every factory required significant remediation before approval, underscores the fundamental challenges of working conditions in the industry.

Since the New Source Approval Process was instituted, all factories with which Nike places orders directly should receive an initial environment, safety and health assessment (SHAPE) and a third-party labor audit, at a minimum. There are times when a factory is not authorized, but manufacturing product for Nike. As a result, unauthorized factories may not have been audited. We also know from anecdotal experience that approximately five percent of our audited factories in FY04 were found to use contractors that had not been formally approved. Unauthorized subcontracting is prohibited by our Code of Conduct.

Stage Two: Monitoring and Factory Remediation

We have three levels of monitoring: Basic ESH monitoring (SHAPE), in-depth M-Audit and independent external monitoring through the FLA (all are described in this section).

Factory remediation and capacity building are described more completely in the section below.

Stage Three: Addressing the Impacts of Factory Exits

In 2002, we decided for a variety of business reasons to cease placing orders with the Indonesian footwear factory, Doson, for whom Nike was the sole customer. As the decision was implemented, ultimately more than 7,000 people lost their jobs. We worked with the factory so they could take a series of steps to ease the impact, including investing in extended health care coverage and job re-training for workers. All workers ultimately received the severance payments owed to them. But we found ourselves making up the exit steps as we went along.

After that experience, we developed a standard factory exit process. Today, when a significant number of workers may be affected by our decision to end our business with a contract factory – a decision that can be driven by a host of business issues including changing consumer demand and falling factory performance – we try to apply this standardized exit process, which was developed in FY04.

The Factory Exit Response Plan calls for Nike to

- Support workers receiving all entitlements from the factory as set out in the labor law
- Advocate to contract factory owners to fulfill all severance requirements as set out in the labor law
- Leverage a wide range of contacts to help move a factory owner toward fulfillment of legal obligations
- Explore worker support programs if the owner fails to meet legal obligations

Given the criteria for applying the factory exit process, i.e., in factories where a reduction in orders would affect a significant number of workers, we have not had to apply this process often. It is possible that we miss some situations where our share of production is sizable enough that a decision to end orders has an impact on worker employment. (This may be particularly true for factories producing Nike products through agents and licensees, where we have less visibility.) But our intention with this process is to apply a high level of responsibility throughout the life cycle of a factory's business relationship with Nike, and to encourage the factory to do the same. We also recognize the relevance that this process may have in the future as we work with Nike product teams to monitor sourcing decisions in the post-MFA world.

ISSUES AND IMPACTS

Monitoring and Audits

Nike employs several basic monitoring tools. The SHAPE inspection, our oldest monitoring tool, used since 1997, provides a basic gauge of a factory's compliance performance including environment, safety and health. The SHAPE inspection is typically performed by Nike's

field-based production staff and can be completed in one day or less. The goal of the SHAPE audit has been to provide a broad picture of our factory base, in contrast to our other main auditing tool, the M-Audit, which provides a deeper assessment of the labor

WORKERS IN CONTRACT FACTORIES

management practices. Although it has been difficult for us to meet this target, our goal in the past was to have two SHAPE audits conducted on each active factory each year. Independent audits conducted by the FLA and our own in-depth environment, safety and health assessments indicate that much work is needed to improve compliance with ESH. Until now, health and safety issues have been covered by our SHAPE audit. We are currently evaluating our auditing process around environment, safety and health based on in-depth audits conducted in FY04 and FY05.

Number of SHAPE Inspections Performed in FY04

Region	Apparel	Equipment	Footwear	Total
Americas	145	26	7	178
EMEA	134	18	5	157
N. Asia	178	112	88	378
S. Asia	208	27	68	303
Total	665	183	168	1,016

In FY03, we began a transition from third-party labor practices monitoring performed by independent contractors to a new, internal monitoring process called the **M-(for “management”) Audit**. We hired 21 new staff, and specifically trained them in labor auditing practices. The M-Audit is now the bedrock of our compliance monitoring activity and our primary tool for understanding our issues and impacts with respect to working conditions. There were several reasons why we decided that it made sense for us to do our own monitoring: quality, consistency and credibility with business colleagues who were going to be asked to make tough sourcing decisions on the basis of their findings.

We hope we can bring our learnings from internal monitoring to future efforts around shared monitoring that will allow for the achievement of greater scale while maintaining quality and consistency.

Number of M-Audits Conducted FY03 and FY04

Region	Apparel	Equipment	Footwear	Total
Americas	110	29	9	148
EMEA	51	4	1	56
N. Asia	101	64	33	198
S. Asia	121	19	27	167
Total	383	116	70	569

	FY03	FY04
M-Audits conducted	278	291
Worker population in audited factories*	374,988	212,760
Worker population in total (active and inactive) factory base	588,678	652,926

**Dates of worker population count: 7/1/03 and 6/4/04.*

**More workers were covered through M-Audits in FY03 due to the focus on factories with a higher risk of non-compliance, which tend to be larger in size.*

The M-Audit is designed to do one thing – uncover problems. Trends identified by the M-Audits have helped us prioritize our work in the area of factory remediation and business integration. This includes a factory walk-through, documentation checks and confidential on-site interviews with individual workers, supervisors and managers. The majority of our audits are announced, but approximately 10 percent of our M-Audits are unannounced.

Contrary to common belief, we feel that our audits are more effective when announced. While it is true that contract factories are unable to prepare for an audit if not given prior notification, we also find that much of the information we require in our evaluation of a factory is dependent upon access to relevant records and individuals within factory management.

Compliance Team

Our compliance team consists of more than 90 people based in 24 offices in 21 countries around the world.

M-Auditors

Of the more than 90 members of the compliance team, there are 46 employees who regularly conduct M-Audits. The typical M-Auditor is under the age of 30, which mirrors the worker population. Approximately 74 percent (34 of the 46) of the compliance staff who routinely conduct M-Audits are women, again reflecting the worker population. We try to hire auditors who are local nationals who have the benefit of understanding the local language and culture. This is particularly important for the worker interviews. In FY03 and FY04, over 9,200 factory workers were individually interviewed as part of the M-Audit process. Each interview took approximately 30 minutes.

In FY04, the typical M-Audit took an average of 48 hours to complete, including travel to and from the factory.

Average M-Audit (time allocation) FY03 and FY04

Audit Process	Total Hours (compliance team)	Average time spent per audit (average number of hours rounded to half hour)	Average time spent per audit (% of on-site hours)
Opening Meeting	492	1.0	3%
Management Interview	999	2.0	6%
Walk-Through	937	1.5	4%
Sample Selection	723	1.5	4%
Records Review	1,530	3.0	9%
Employee File Review	1,178	2.0	6%
Hours/Wages Review	3,817	6.5	19%
Worker Interview	4,599	8.0	23%
Supervisor Interview	558	1.0	3%
Grading Instrument	985	1.5	4%
Audit Summary	876	1.5	4%
Closing Meeting	1,189	2.0	6%
Administrative Time	1,651	3.0	9%
Total On-Site Audit Hours	19,534	34.5	100%
Travel Hours	7,703	13.5	
Total Hours (Audit & Travel)	27,237	48.0	

M-Audit hour's calculations as recorded by Nike compliance in FY03 and FY04.

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The M-Audit was designed to give us a deeper understanding of the working conditions within contract factories, with a bias toward factories with a higher risk of non-compliance.

Our non-compliance risk assessment for factories (which determines the likelihood of a factory receiving an M-Audit) is based on the following:

- The **country of manufacture**, to account for countries with poor standards or lax enforcement
- The **size of the worker population**, because larger factories mean more people affected by potential non-compliance
- The **nature of manufacturing**, because non-compliance in factories using more solvents or heavy machinery puts workers at a greater potential risk
- The **past compliance performance** of the factory or its ownership team, which tends to be better in factories where we have had long-term business relationships

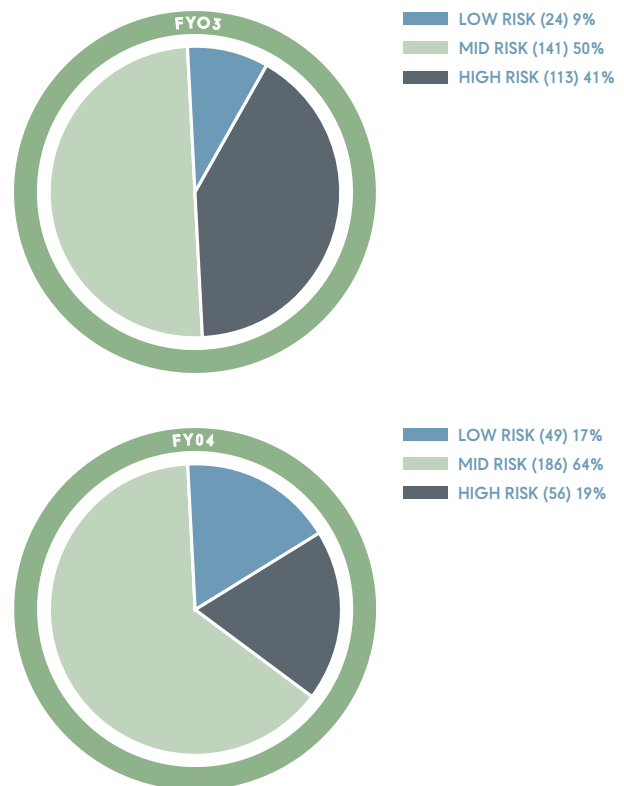
Once inside the factory, our M-Audit team is instructed to focus on the following:

- **Factory processes and policies.** Factories are graded on processes and policies, as well as outcomes. If the factory has a sub-standard policy or process, it is rated non-compliant even if there is no evidence those management practices have created negative impacts for workers.
- **Worker views** through one-on-one confidential interviews. Workers are selected from job categories that are likely to be subject to, or witness to, non-compliance events. Effective worker interviews are critical for understanding the actual conditions of work within a factory.

With the M-Audits, our goal has been to cover approximately 25-33 percent of our active factory base each year. In FY03, our first year of the new M-Audit process, we focused audits on factories presumed to have the highest risk of non-compliance and the greatest size (as measured by worker population). In FY04, we shifted to factories we believed were of medium risk.

Some of the low-risk factories may receive less monitoring. For example, factories located in highly regulated countries, where workers are more informed about their rights and the laws are enforced, are often categorized as low risk, and we have chosen to focus our resources on contract factories where workers are less protected.

M-Audits conducted by level of non-compliance risk



Independent Monitoring

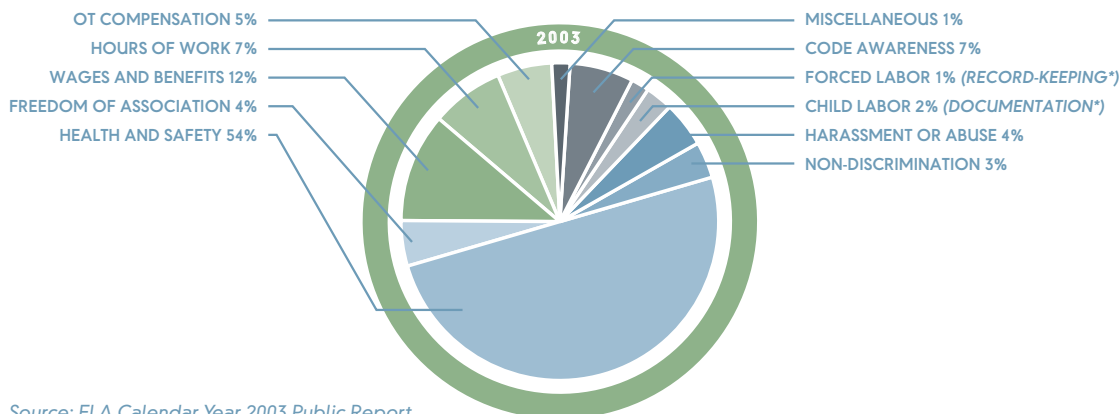
We rely on independent monitoring conducted through the Fair Labor Association (FLA) to provide us with an external perspective of working conditions in our supply chain.

The FLA, of which Nike is a participating company, is a consortium of brands, universities and NGOs. The FLA accredits independent monitors to perform unannounced audits of five percent of our supply chain each year. This amounted to 40 independent audits of Nike factories in FLA Year Two (2003). For each member, the FLA reviews audit findings, oversees

remediation efforts and internal compliance processes, and reports publicly on all of these activities. Nike entered a three-year accreditation process in 2003, and the FLA will make its decision when that period ends in the late spring of 2005. This accreditation

process represents an independent review of our internal systems and processes for managing compliance for all product categories – apparel, footwear and equipment. The FLA 2004 Annual report can be found at <http://www.fairlabor.org/2004report>.

FLA audit findings for 40 Nike contract factories (Issue percentage as percentage of all issues found)



FLA Independent External Monitoring Findings

The figure above displays the percentage breakdown by Code Provision of the total non-compliance issues reported by FLA independent monitors in Nike applicable facilities, which Nike addressed through remediation in Year Two. Non-compliance findings relating to Health and Safety were the most frequently reported issues, making up 54 percent of the total non-compliance issues identified¹. The most commonly reported and remediated Health and Safety issues related to inadequate postings and evacuation procedures, and personal protective and safety equipment.

Issues related to Hours and Wages were also common, with a total of 24 percent of all findings relating to Wages and Benefits (12 percent), Hours of Work (seven percent) and Overtime Compensation (five percent). The top Hours and Wages issues that were reported by FLA monitors and taken up by Nike through corrective action plans were related to overtime limitations, overtime compensation and worker awareness of their wages and benefits.

There were no findings of underage workers in facilities producing for Nike. Issues categorized under the Child Labor provision (two percent of all non-compliance reported) mainly related to factories having inadequate documentation for workers' ages in factory records, as required by the FLA.

There were no findings of forced or bonded labor in these facilities. Most non-compliance issues categorized under the Forced Labor provision (one percent of all non-compliance reported) related to factories keeping inadequate records to demonstrate compliance with all FLA benchmarks for this provision.

Source: www.fairlabor.org

**Text in italics has been added by Nike for clarification purposes.*

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As discussed in previous sections (of the FLA Report), the FLA is working to develop systems for more effective monitoring and remediation of the Code Provisions that are particularly complex and difficult to assess, such as Freedom of Association and Collective Bargaining, Non-discrimination and Harassment and Abuse.

Source: The FLA Website at http://www.fairlabor.org/2004report/companies/participating/factoryData_nike.html. It should be noted that two percent of FLA audited issues involving child labor referred to improper documentation of age. None of the FLA findings indicated underage workers.

Root Cause Analysis

The limitation of most monitoring tools is that they identify problems, but are often inadequate in identifying root causes. For example, to understand overtime, one must examine the buyer-seller relationship, including manufacturing timelines, pricing, quality demands and their associated downstream impacts on the worker. We need to understand better how our business decisions may contribute to negative impacts on workers.

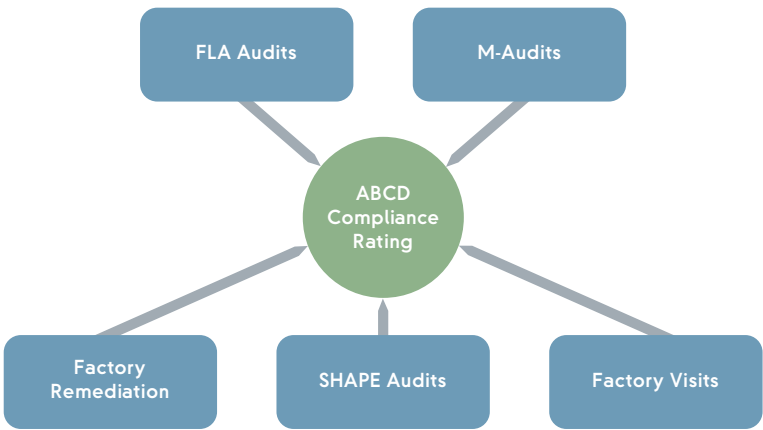
In FY05, a group of Nike contract factories are opening their doors to research teams from the Sloan School of Management at the Massachusetts Institute of Technology (MIT), who will examine a range of questions around the business drivers and outcomes. We hope to gain insights about the whole of the business process, which should help Nike and contract factories better manage production flows and factories manage hours of work. In addition, we are currently working with external parties to look

at some of these issues more deeply in the areas of environment, safety and health.

BUSINESS INTEGRATION

Key to integrating concepts of incentives or sanctions into our sourcing and production is the ability for us to assess the extent to which a contract factory is compliant with our code.

To facilitate this, we have developed a grading system. The letter rating, which reflects all of our relevant information about a factory's compliance performance, is assigned by the field compliance manager and reviewed by the regional director. It is derived from the number and nature of non-compliance issues discovered by various forms of monitoring and oversight (SHAPE inspections, FLA audits, factory visits and M-Audits where conducted) as well as the resolution of items for factory remediation.



Compliance Rating Criteria

Grade	Compliance Rating Criteria	Description
A	No more than five minor issues outstanding on the Master Action Plan <i>and</i> no more than 20 percent of MAP items past due.	<ul style="list-style-type: none"> Non-compliance issues that do not reach levels defined as C or D issues (see below).
B	More than five minor issues, but no serious or critical issues outstanding on the MAP <i>and</i> no more than 30 percent of MAP items past due.	<ul style="list-style-type: none"> Non-compliance issues that do not reach levels defined as C or D issues (see below).
C	One or more C-level issues, but no D-level issues, outstanding on the MAP <i>or</i> more than 30 percent of MAP items past due.	<ul style="list-style-type: none"> Lack of basic terms of employment (contracts, documented training on terms, equal pay, discriminatory screening) Non-compliance to local laws on treatment of migrant workers Less-than-legal benefits not related to income security (e.g., leave) Excessive hours of work: greater than 60 hours/week but less than 72 hours/week Exceeding legal annual overtime work hour limit for 10 percent or more of the workforce Not providing one day off in seven Verbal or psychological harassment or abuse Conditions likely to lead to moderate injury or illness to workers Conditions likely to lead to moderate harm to the environment or community
D	One or more D-level issues outstanding on MAP <i>or</i> Serious issues past due; <i>or</i> more than 40 percent of open MAP items past due.	<ul style="list-style-type: none"> Unwillingness to comply with Code standards Denial of access to authorized Nike compliance inspectors Falsification of records and coaching of workers to falsify information Homework, or unauthorized sub-contracting Underage workers Forced labor: bonded, indentured, prison Denial of worker rights to Freedom of Association where legal Pregnancy testing Confirmed physical or sexual abuse Paying below legal wage Denial of benefits tied to income security No verifiable timekeeping system Exceeding legal daily work hour limit or work in excess of 72 hours/week for 10 percent or more of the workforce Not providing one day off in 14 days Conditions that can lead to death or serious injury Conditions that can lead to serious harm to the environment

WORKERS IN CONTRACT FACTORIES

A factory can receive a C or D rating if non-compliance is discovered in one or more of the issues listed above. For example, a factory may have an exemplary compliance record, but if only one instance of unauthorized sub-contracting is found, that factory will nevertheless receive a D rating.

It is our aim to move factories with a C or D compliance rating to a higher rating within three to six months, respectively. If we feel that a C- or D-rated supplier is not making adequate progress in meeting their remediation targets within the set timeline, we will

re-assess our business relationship. Because this is a new system, and there is still a level of inconsistency in our assignment of ratings and additional work needed to notify factories and production staff about the consequences of receiving D ratings, we have not yet instituted hard deadlines for compliance. For this system to work, we also need to find a solution to the challenge of completing timely follow-up visits to confirm factory claims of completed remediation. This is an area where shared industry collaboration could have an impact.

Non-Compliant Factories

We work hard to help our contract factories implement remediation of non-compliance items found during our audits, regardless of the severity of the initial findings, but there have been cases when the behavior of factory managers has demonstrated their lack of commitment to this process and we have been forced to terminate relationships.

A factory is cut from our supplier base when, over a period of time, it lacks the capacity or the will to correct serious issues of non-compliance. One supplier in China, for example, was cited for repeated violations of overtime standards and falsification of records. The compliance team established action plans, which three different Nike business units worked with the factory to implement. After six months of continuous efforts, and no improvement, the factory was dropped.

More typically a decision to end a business relationship is based on a combination of issues. In FY04, a manufacturing group in South Asia was performing poorly on a range of issues, from overtime and worker/management communication to the quality of product and shipping dates. After a series of performance reviews, the factory group was informed that we would not be placing orders for the next season. We do not report on factories dropped for compliance reasons because it is often difficult to isolate poor performance on compliance as the sole reason for terminating a business relationship.

The Balanced Scorecard

If much of our work to date has focused on understanding the issues, we now have a tool designed to drive change and move us closer to our goal of achieving a sustainable sourcing strategy. Our Balanced Scorecard gives us an opportunity to reward high-performing factories. It is key to our business integration strategy.

We have adapted a traditional business tool – the balanced scorecard – to help us track and assess the corporate responsibility performance of Nike's footwear and apparel divisions. Within one of the broad categories covered by the scorecard – operations – we have identified four processes that must also be balanced.

Three of these processes – cost (what Nike pays for the product), delivery (receiving the product on time) and quality – represent the standard decision-making tool in our industry; it's how orders are nearly always placed. The numbers are easy to track in real time, and most factories and production managers have been judged on their ability to hit targets for these processes. If the factory hits the target, they get more orders. With the fourth process compliance, we've added an important change in how orders can be placed. Our current metrics for gauging progress are more subjective than the three standard measurements, and are reported monthly. But by providing measurable targets, we alter the equation and can begin providing incentives to our factories and our own production staff for compliance performance.

Compliance performance is tracked in the form of our compliance rating based on an ABCD scale (see chart on page 25). This system helps us document and communicate compliance issues throughout the business.

Once the letter is assigned, it is slotted into the Balanced Scorecard and is nested next to other, more

traditional measures of performance: quality, on-time delivery, price and compliance. In addition to using this system to reward the best factories, we also plan to use it as a management tool for those factories needing the greatest improvements. We have found compliance ratings generate growing visibility around non-compliant factories and achieve increasing levels of responsiveness from our business units. As a result, even as we shift our resources to a greater focus around factory remediation and capacity building, monitoring will continue to be a pillar of our strategy for integrating compliance into our business.

The Balanced Scorecard has helped us understand the interrelationships of our categories of measurement. We've long known that pushing too aggressively in one area can disrupt the balance and have consequences elsewhere. We also believe that the balanced scorecard is an effective tool for communicating internally to our production staff and externally to our contract factories the importance we place on achieving balance between cost, quality, compliance and delivery.

Working with Contract Factories

Our supply chain has evolved in recent years. We have built strategic relationships with manufacturers who have the capability to support us in delivering technical performance product. The goal of this approach is to build a collaborative relationship based on mutual success, identify the changes that can be made to increase the efficiency of our supply chain and to improve factory performance across all dimensions of the balanced scorecard, including compliance. We believe that we no longer need to rely on confidentiality to secure our relationships with key suppliers; this relationship will be protected through better business practices and mutual interest. Our contract factories are also gaining a better understanding that their reputation is best maintained through investing in CR as a point of differentiation in attracting long-term buyers. Public disclosure of our contracted factories should promote suppliers that have greater ownership of their own reputation as a means of competitive advantage.

Our production managers are beginning to see how their decisions may have a downstream effect on working conditions. We've found, for example, that pressure on the delivery schedule can contribute to

non-compliance with our standards. That is, if we are late in delivering product specifications or materials, but still expect a product delivered on time, the factory manager may choose to rely on more overtime.

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Although we hope to do a better job of building incentives for factories to improve in corporate responsibility via the scorecard, it is a balanced scorecard. This means that if a factory has made significant improvements in compliance but not in other areas, we may decide not to continue placing orders with that factory. Conversely, factories may perform well on cost and delivery or provide us with unique product, but have a poor track record on compliance. In these cases, our work is focused on assisting with their remediation efforts of non-compliance.

We recognize that a key component driving the effectiveness of this system lies in placing accountability within employee performance evaluations for decisions affecting compliance. Moving forward, we will be looking at the right tools for embedding accountability and aligning incentives within the business to support our corporate responsibility goals.

Factory Remediation

When a factory is found to be out of compliance with the code, the compliance team works with factory management and the Nike business unit to develop a Master Action Plan (MAP) to guide the factory's remediation efforts.

When remediation works best, it involves Nike compliance staff, production staff and management, as well as managers from the contract factory. The factory management team attends the M-Audit closing meeting, reviews the results, drafts its own MAP, provides it to Nike, and begins correcting issues identified by the compliance team. The Nike production manager responsible for the business relationship with the factory monitors progress and exchanges information about progress or obstacles with the country compliance team. The Nike general manager for production monitors the progress of all factories within his or her purview, and weighs in when factory remediation progress is too slow.

Factory remediation is helped along by our compliance team through their regular visits to factories, which supplement the 1,016 SHAPE Audits conducted in FY04 and in-depth M-Audits at select factories. The typical Nike compliance team in each country spends about one-third of their time on monitoring and auditing activities, about half their time assisting and tracking factory remediation activities, and the remainder of their time on trouble-shooting and collaboration/outreach work.

The MAP defines the *who, what, when* and *how* of remediation. Currently, the MAP contains every item identified as a non-compliance issue, from a fire extinguisher that has not been checked to unpaid wages and overtime hours in excess of our code. Some MAPs may have fewer than 10 items and others may have dozens of items both major and minor. Going forward, we will focus our follow-up on priority issues that we believe will have the greatest effect on improving conditions for workers. Another challenge we face is making sure remediation sticks. We have found that the episodic improvements

identified by our compliance team often re-emerge as non-compliance findings in subsequent audits.

For example, a MAP item around non-compliance with payment of erroneous wages would include instructions to pay the proper rate of pay going forward and reimburse the worker for wages owed for up to one year.

Remediation progress is not always linear, swift or complete. In areas of non-compliance where progress is easy to measure, it can be. Workers fired without just cause or due process, for example, can be re-hired, and

we can document it. Underpaid wages can be corrected and verified. Hours of work above Nike's standard can be adjusted downward and checked against time clocks, worker interviews and observation.

But with an average of one compliance staff for more than 10 factories – some of which are remote and some of which are large and complex businesses with 10,000 people or more – constant monitoring, tracking and assisting factory remediation is at times an overwhelming and incomplete body of work. This is one area where the open-source model of compliance has enormous potential. Transparency across the industry of our respective contract factories will promote greater collaboration, sharing of monitoring information and reinforcement of remediation expectations across the industry. This could also decrease the burden on suppliers dealing with contradictory audit requirements by multiple buyers.

Training and Education

While remediation focuses on addressing specific findings of non-compliance, training enables us to

build our capacity and that of contract factories to implement and sustain improvements.

Where technical assistance is needed, including interpretation of standards or issues, members of the Nike compliance team may visit the factory and provide the necessary support. The team also provides generalized training, or makes it available through outside resources, to raise factory team competencies and capacities to self-manage labor, environment, safety and health.

Among those areas of training and education we believe have been most significant in FY04, and continue in FY05 include the following:

- A global effort to raise factory awareness of labor law and Nike standards, often involving local labor experts
- A parallel global effort to raise factory awareness of environment, safety and health (ESH) management, focusing on ESH committees
- Building our own staff competencies to assist contract factories with remediation

Remediation in Action

A high-volume Turkish supplier with a history of marginal compliance with the Nike code turned its performance around when we took active steps to assist with remediation. We started by taking a step back from the symptoms in the factory and asked factory management to apply their management approach for other areas of their business to compliance issues. The resulting management restructure and creation of a management system within the factory led to notably improved working conditions in the factory. We are hopeful the management's plans to feed this out into their subsidiaries and subcontractor base will achieve long-term improvements broader than just the one factory.

Another contract factory, located in Egypt, was found to be non-compliant with our standard around benefits. Management had failed to register its employees under the government social security system – a common industry problem. Although the factory manager knew of the benefits and requirements of such registration, no progress was made. Rather than pursue this as a compliance issue alone, our compliance team involved the Nike business team responsible for liaising with the factory in the next compliance meeting. Seeing that this was not only a legal requirement but a Nike business requirement convinced the factory manager to register all his workers, including himself. Since then, the factory manager has commented that even he is happier and feels that he is more secure at work.

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In FY04, we documented more than 16,000 individual workers or managers who received some form of compliance training from Nike, on topics ranging from safe chemical handling practices and personal hygiene

to how to manage an internal grievance system. The largest individual body of training was performed under the auspices of the Global Alliance for Workers and Communities (see below).

Nike-hosted Training FY04	Number of attendees
Factory Workers and Management (total)	16,590
• Environment, safety and health training	2,137
• Labor-related training	14,453
External Auditors: pre-source audits, M-Audits and SHAPE	119
Nike Employees: (Environment, Safety and Health and SHAPE)	72

Worker Development and The Global Alliance

One of our most important partners in understanding factory worker concerns and in the provision of training to both workers and managers has been the Global Alliance for Workers and Communities. After five years of operations, its partners collectively chose to end the initiative in December 2004.

The Global Alliance was a partnership of Nike, Gap, the World Bank, the International Youth Foundation (IYF) and other organizations aimed at worker and workplace development. Since its launch in 1999, Global Alliance facilitated interviews with more than 16,000 workers and launched a number of development projects focusing primarily on building better management practices and worker awareness of health issues. The Global Alliance interviews and focus groups also helped us to uncover the kinds of compliance issues that were difficult to bring out in typical audits, such as sexual harassment and overall satisfaction with the work environment. In FY04, the Global Alliance trained more than 25,000 workers and managers in more than 60 factories in China, India, Indonesia, Thailand and Vietnam.

The Global Alliance was criticized in some quarters as, at best, irrelevant when compliance issues abound and, at worst, an end-run around trade unions. We believe this dismissal of the Global Alliance misses a larger point; though not a perfect effort, the five-year experience with the Alliance taught its partners a great deal about worker issues and aspirations, and highlighted some core compliance issues as well.

We would not have a heightened awareness of harassment issues were it not for the Global Alliance. We know that to get a deeper understanding of a workplace, we must go beyond M-Audits scores and probe under the surface to try to measure worker satisfaction with the workplace.

Work done with the Global Alliance in Indonesia is a useful example of where we believe progress was made through our approach to compliance. Following revelations of widespread compliance abuses, our team worked with the factories in question to develop a comprehensive remediation plan. A subsequent alliance report demonstrated that improvements were made to the factories. Please see <http://www.theglobalalliance.org>.

Although we were able to gather anecdotal information about some of the positive impacts of the Global Alliance on the workplace, particularly the management training and worker health training, a measurement of actual impacts is still to come. A final study examining the knowledge from the Global Alliance is being compiled and will be made available to the public upon completion. The Global Alliance's inability to expand programming and attract other corporate partners proved limited, which led to the decision to end the initiative.

At this point in time we are exploring different ways to use the remaining Global Alliance funds in the spirit of the Alliance. We will report on this in the FY05 report.

In addition to the Global Alliance training, Nike continues to co-sponsor, with factory management, a program of worker after-hours education generally aimed at securing a high school equivalency for workers in footwear factories in Thailand, Vietnam, Indonesia and China. In the 2003/2004 school year, 984 workers graduated from one of those programs. Our commitment to worker and workplace development remains.

Global Alliance Training and Worker Development Programs

Global Alliance (Nike FY04)	Number of Attendees					Total
	China	India	Indonesia	Thailand	Vietnam	
Management Training	2,953	228	1,553	808	812	6,354
Project Team Member Training	796	34	90	178	–	1,098
Interpersonal Relationship	–	2,400	–	–	–	2,400
Health Training	890	5,842	372	1,643	212	8,959
Other Training	7,700	84	–	142	–	7,926
Health Fair	4,000	–	–	–	14,400	18,400

MULTI-STAKEHOLDER INITIATIVES AND INDUSTRY CHANGE

We hope that our disclosure of our supply chain will spark a new level of multi-stakeholder collaboration and industry change. A description of some of the efforts we have engaged in to date follows below.

Global Multi-Stakeholder Initiatives

Six Codes Initiative

We have long believed in the need for common reporting and auditing standards. Our initial reason was that it would allow for comparisons between companies, but we see other, more important reasons for the common platform.

Currently, many brands often pay to monitor the same facility with their own separate auditors, standards and priorities. This is wasteful and ultimately takes funds and attention away from higher priorities, such as helping factories build internal management capacity, sharing best practices, and learning from one another. It also places a significant burden and cost on factories. One contract factory in Europe was audited more than 40 times in one year by its different buyers and their compliance personnel – a significant interruption of workflow.

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The challenge of meeting different standards can be highlighted with a simple example: Different work codes call for different placements of fire extinguishers. To stay in compliance, one factory might need to have the fire extinguisher mounted five feet high on a wall for one company's audit, four feet high for a second company's audit, or on the floor for a third one. Picking one of the standards and sticking with it means the factory is out of compliance with the other two audits. This borders on the absurd.

If monitoring becomes standardized, and we can achieve consistency in the quality of audits, it should follow that it will be quicker and cheaper to acquire compliance data and to achieve broader coverage.

Our first step toward harmonizing our compliance standards with those of other companies came through the American Apparel Industry Code of Conduct, established at the invitation of the Clinton administration in 1997. This effort led to the creation of the Fair Labor Association, whose membership now includes more than two dozen brands, a number of NGOs and over 175 universities with licensed apparel programs. These companies include American, European and Canadian brands whose total annual revenues amount to approximately \$30 billion. Despite the steps taken by this small group of companies, this group accounts for just a fraction of the global apparel and footwear industries, which were valued at \$935.1 billion and \$284.4 billion respectively in 2004 (Datamonitor 2004).

There are at least five other major compliance and monitoring organizations with established codes of conduct. The next generation of harmonization will focus on bringing these initiatives, including the FLA, into better alignment. One step in that direction is an initiative of six code-based organizations focused on developing a common standard and then testing the monitoring and remediation of that

code, using factories in Turkey as the test base. The six organizations, which will issue a public report on the results, are as follows:

- Clean Clothes Campaign
- Ethical Trading Initiative
- Fair Labor Association
- Fair Wear Foundation
- Social Accountability International
- Workers Rights Consortium

Global Reporting Initiative Sector Supplement

A separate but similar initiative is based on our belief that increased transparency and standardized reporting will serve as an effective mechanism for continuous improvement in our industry. This initiative involves collaboration with the Global Reporting Initiative and industry colleagues and stakeholders to establish a working group to agree upon a uniform set of reporting guidelines for the apparel and footwear industries.

MFA Forum

The MFA Forum was formed by a small group of stakeholders following discussions that occurred at Nike's 2004 stakeholder forum. This group subsequently expanded to include multiple brands, trade unions, NGOs and international development institutions with collective concerns about the potential impact of the quota phase-out on workers. This group ultimately became the MFA Forum. Outputs of this forum include in-depth research and a Collaborative Framework for Guiding Post-MFA Actions. Going forward, this forum will serve as a facility for promoting and sharing experiences in collaborative initiatives that address the challenges emerging from the end of the MFA. This facility will be modest and time-bound, and will comprise the following elements: (a) *Basic information exchange* about post-MFA related collaborative initiatives at the country, regional and international levels; (b) *Promote learning* about the effectiveness

of such initiatives through participation in and hosting relevant forums, supported as required by more formal research; and (c) *Inform, initiate and facilitate specific collaborative initiatives* by networking relevant actors and facilitating the initial stages of in-country collaborative initiatives where appropriate.

For more information on MFA, see the *Challenges and Opportunities* section.

PERFORMANCE

Writing this report has been a process of introspection. It has also been a process of internal transformation that led us to the decision to disclose our factory base.

We know that the M-Audit has provided us with very robust data on the major issues of non-compliance that exist in our supply chain, which has led us to identify four priority areas to focus our energy on going forward within the management of labor issues:

- Freedom of association
- Harassment, abuse and grievance procedures
- Payment of wages
- Hours of work

Our understanding of these issues and activities taken around them is described in greater detail below.

The M-Audit does not produce a meaningful comparison of improved or declining performance, i.e., or the extent to which remediation is occurring, and conditions improving. While we have anecdotal evidence, we realize that our ability to measure improvements is another challenge for the future. Many of our stakeholders have pointed out that we have many measures of activity, but less ability to measure impact. Consequently, we are currently re-evaluating our metrics for measuring the impact of our compliance efforts.

Until recently, we thought a robust monitoring program would be an effective means of assessing our contract factories' progress year-on-year in complying with our Code of Conduct. We have come to realize that our monitoring scores are perhaps a better reflection of our success as monitors than an accurate assessment of performance over time. This is consistent with industry colleagues who report significant increases in non-compliance from their baseline data.

We have also concluded that because monitoring does not necessarily lead to factory remediation, we need changes in the underlying system that would enable us to shift more of our resources to capacity building. It is our hope that the collaboration resulting from additional supply chain disclosures by our industry colleagues will enable this shift.

The results of our audits do, however, provide useful information to feed into our compliance ratings (ABCD) that will serve as the basis for our efforts toward internal business integration and factory remediation.

Fiscal year 2004 was our first year to apply letter ratings to our contract factories as a mechanism for communicating compliance performance to our production staff. As this represents our baseline, we are not yet certain what rating distribution we should expect across the source base. One finding of non-compliance with a critical issue causes a factory to receive a D rating. One finding of non-compliance with a serious issue causes a factory to receive a C rating. As we continue to refine these rating assignments, it is likely that a growing number of factories will fall within our C and D categories.

Despite the rigor of our new source approval process, we are finding that significant numbers of factories receive C and D ratings. We believe this reflects the reality that many of the factories in our supply chain were active prior to the development of our New

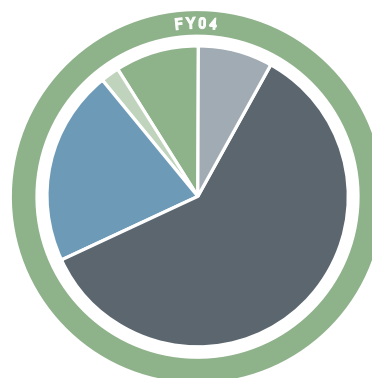
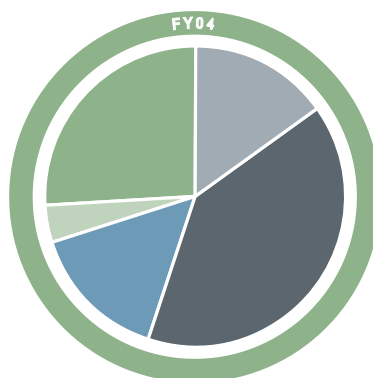
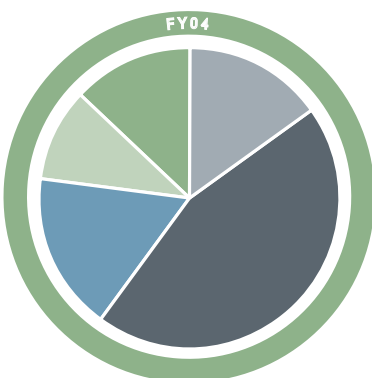
WORKERS IN CONTRACT FACTORIES

Source Approval Process. It also reflects the reality that change is a long process that starts with educating factory managers and workers. It is sustained by building the knowledge and skills to improve and maintain decent working conditions.

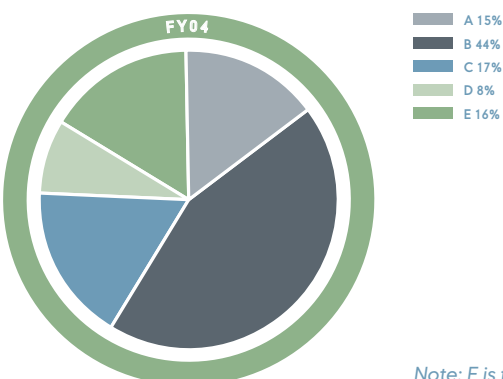
At the close of FY04, using definitions developed for each rating, ABCD, we updated or assigned new ratings to factories in the source base. The following chart displays the most current contract factory compliance ratings.

Nike Brand Active Contract Factories Compliance Ratings (June 4, 2004)

	APPAREL					EQUIPMENT					FOOTWEAR				
	A	B	C	D	E	A	B	C	D	E	A	B	C	D	E
Americas	23	49	17	4	9	9	8	1	0	8	0	7	0	1	1
EMEA	11	34	5	32	5	3	4	2	3	2	1	2	0	0	0
N. Asia	21	78	16	9	8	9	48	16	5	14	4	21	3	0	0
S. Asia	21	60	48	2	45	4	7	6	0	20	0	9	11	0	5
Total	76	221	86	47	67	25	67	25	8	44	5	39	14	1	6



ABCDE Compliance Rating Globally



Note: E is for unrated factories due to insufficient information.

M-Audit Findings

Each M-Audit generates a numeric score that represents a percentage against 100 percent compliance, with 100 indicating full compliance. This score allows us to get a more comprehensive baseline picture of where a factory stands at the time of the audit. As noted previously, the M-Audit score is fed into the

overall grading of a factory, and is also used by factories as a tool for building master action plans.

The following chart displays the range of aggregate M-Audits scores for the 569 contract factories that received M-Audits in FY03 and FY04.

M-Audit Scores (FY03 & FY04)

		Combined	Apparel	Equipment	Footwear
Americas	Lowest Score	46	46	59	46
	Average Score	78	78	81	68
	Highest Score	94	92	94	81
EMEA	Lowest Score	49	50	49	73
	Average Score	70	69	73	73
	Highest Score	96	92	96	73
N. Asia	Lowest Score	25	26	29	25
	Average Score	61	61	56	71
	Highest Score	99	89	85	99
S. Asia	Lowest Score	20	20	33	28
	Average Score	58	56	64	60
	Highest Score	95	88	96	95
Global	Total # of Audits	569	383	116	70
	Lowest Score	20	20	29	25
	Average Score	65	66	64	66
	Highest Score	99	92	96	99

The M-Audit is divided into four major categories of inquiry – hiring practices, worker treatment, worker-management communications and compensation. The M-Audit currently covers more than 80 labor-management issues, with each issue accounting for a specific weighting with respect to the overall grade.

The chart that follows displays the range of non-compliance by specific issue across the full set of issues covered by our M-Audits. A factory is found to be non-compliant if our auditors find one or more incidence of factory conduct that does not meet our code standard. In effect, the numbers report rates of incidence, but not breadth or severity of impact. We will be looking at how to better capture breadth and severity in more depth in the coming year.

Non-Compliance Findings at 569 M-Audited Factories (FY03 & FY04)

ISSUES		AMERICAS	EMEA	N. ASIA	S. ASIA	TOTAL
Hiring Practices	Process Control	Age verification process inconsistent or not well documented				
		Applicants are asked to disclose non-job-related information (e.g., marital or family information)				
		Voluntary nature of the employment is not documented				
		Eligibility to work document is not kept or inconsistently maintained				
		Legally required employment documents for workers are incomplete				
		Mandatory overtime policy communication to managers is not documented				
		Mandatory overtime policy communication to workers is not documented				
		Mandatory overtime policy communication is not provided				
		Unapproved subcontractor used				
		Wage penalty imposed if resignation notice is not adequate				
		Young Workers (less than 18) are not fully informed of legal protections for work conditions and hours				
	Outcome	Age below legal minimum				
		Age below Nike Standard (Footwear 18, Apparel/Equipment 16)				
		Female applicants are required to undergo pregnancy test				
		Home work is practiced				
		Forced labor				
		Original documents (e.g., travel documents, personal I.d.) withheld from workers as a condition of employment				
		Security deposit required for employment				
		Workers are required to pay for tools (e.g., scissors)				
		Young Workers (less than 18) are not provided with legally mandated medical checks				
Treatment of Workers	Process Control	Code of Conduct posting is insufficient				
		Code training for managers is insufficient				
		Code training for workers is insufficient				
		Language and culture training for expatriate managers is insufficient				
		Language and culture training for expatriate managers is not documented				
		People management skill training for managers/supervisors is insufficient				
		People management skill training for managers/supervisors is not documented				
		Non-discrimination policy is not written or does not sufficiently include all required elements				
		Non-discrimination policy posting is insufficient				
		Non-discrimination policy training is insufficient				
		Non-harassment and abuse policy is not written or does not sufficiently include all required elements				
		Non-harassment and abuse policy posting is insufficient				
		Non-harassment and abuse policy training is insufficient				
	Outcome	Workers are not sufficiently aware of basic Code provisions				
		Employment decisions (e.g., promotion) are made based on factors other than job performance				
		Security searches are intrusive				
		Abusive (e.g., verbal, physical) treatment				
		Factory restricts worker egress during non-work hours				
		Factory restricts worker egress for medical or personal emergencies during work hours				
		Factory restricts drinking water or toilet access during work hours				
Worker-Management Communication	Process Control	Union representatives are not elected by workers or workers do not know their union representatives				
		Confidential grievance channel is not provided				
		Grievance system is not effectively managed or process is not well-documented				
	Outcome	Workers were coached to respond positively to auditors				
		Freedom of association is restricted by law (e.g., China, Vietnam)				
		Freedom of association is restricted due to exclusive union agreement				
		Freedom of association is not provided where legal				
		Workers do not trust the grievance process				

Non-Compliance Findings at 569 M-Audited Factories (FY03 & FY04)

ISSUES		AMERICAS	EMEA	N. ASIA	S. ASIA	TOTAL
Work Hours	Process Control	Business operations lead to work hours in excess of 60 per week				
		Legally required overtime permit is not obtained				
		Legally required overtime permit is not posted in the workplace				
		Voluntary signature sheet for work hours exceeding 60 per week is inadequate				
		Timekeeping system or payroll records are not accessible to auditors				
		Timekeeping system for workers to record their hours of work is not provided				
		Timekeeping system data is not used to calculate wages				
		Timekeeping system minute tolerance exceeds Nike standard				
		Regular work hours and overtime hours are not kept in the same timekeeping system				
		Work hours information training is insufficient				
		Work hours information training is not provided or not documented				
	Outcome	Overtime refusal results in penalty				
		One day off in seven not provided				
		Work hours exceed legal limit for pregnant or nursing workers				
		Work hours exceed legal limit				
		Work hours exceed Nike standard				
Wages	Process Control	Piece rate record is insufficient				
		Wage information training is not provided or insufficient				
		Voluntary wage deduction authorization is not well-documented				
		Wage slip information is insufficient				
		Wage slip is not provided				
	Outcome	Probationary period exceeds Nike standard				
		Probationary wages do not meet Nike standard				
		Wage below legal minimum				
		Wage calculation is inaccurate				
		Wage paid off-clock				
		Wage payments are made late				
		Disciplinary fines are imposed				
		Overtime rate is less than legal or calculation is inaccurate				
		Voluntary savings program are not refunded or refund payment is not well-documented				
Wages for switched work days or hours are not calculated properly						
Legal withholdings are inaccurate or not deposited in legally designated accounts						
Benefits	Process Control	Labor law describing legally mandated benefits is not posted				
		Leave policy is not written or incomplete				
		Benefit information training is insufficient				
	Outcome	Personal leave is difficult to take				
		Legally mandated leave(s) not provided				
		All legally mandated benefits are not provided				



Footnote 1: Because M-Audit results reflect rate of incidence not the breadth or depth of an issue in any one factory, audit findings are noted by ranges (i.e., 10%>25%) rather than absolute percentages.

Footnote 2 (under freedom of association): Because of the difficulties associated with monitoring freedom of association, we believe this figure may be under-reported, but likely within the range specified above.

WORKERS IN CONTRACT FACTORIES

Space in this report does not allow for a full treatment of the more than 80 M-Audit issues. What follows is an examination of the findings with regard to the five compliance issues where, we believe, there is greatest concern. Identification of these issues is based on industry benchmarks of audit findings, consultation with stakeholders and our own understanding of which issues are likely to have the greatest effect on workers.

To understand trends uncovered through our monitoring efforts, we examined the findings of various industry organizations regarding patterns of labor non-compliance. While wide variations in auditing tools and auditor quality make it difficult to compare the exact conditions, we discovered in our active factory base with those in another company's data released by the Fair Labor Association suggests that the general trends in noncompliance are consistent (<http://www.fairlabor.org/2004report/overview/iemFindings.html>).

We identified the following topics for in-depth coverage in this report:

- Freedom of association
- Harassment, abuse and grievance systems
- Hours of work
- Payment of wages
- Child labor

Freedom of Association and Collective Bargaining

Protecting the rights of workers to freely associate

and collectively bargain is a responsibility we take seriously. Freedom of association provides workers with the choice to form or join organizations, including trade unions, or not to do so. It is often through forms of collective action that workers can gain the strength they need to pursue or defend other worker rights, including the ability to bargain collectively for improved wages and working conditions.

We believe that when workers and managers have access to constructive dialogue mechanisms within formal trade unions or other structures, then our role as a policing body will become less necessary overall.

At the country level, legal or political constraints often prohibit or limit the right of workers in this area; this is the case in several countries where our product is manufactured. When the law itself prohibits the right of workers to freely associate or bargain collectively, e.g., in Vietnam and China, our goal is to facilitate a process where workers can achieve parallel means of representation. Some believe that this is increasingly possible in Vietnam, where the trade union structure is developing the flexibility to allow for some worker representation at a higher level.

Legal restrictions are also an issue in export processing zones where workers often have the right to freely associate, but the rules may not provide legal protection should they attempt to exercise this right.

Union Representation in Contract Factories

In FY03 and FY04, our M-Auditors reported that more than 27 percent of the audited factories had union representation – trade, exclusive or government affiliated – and an additional 18 percent had worker committees. It is important to note that this does not represent an evaluation of the quality or legitimacy of this union as an independent, elected bargaining body for workers.

Protecting the right to freedom of association is among the toughest challenges our industry faces because

of scale of non-compliance on this issue. Examples of non-compliance include factories that were found to

have actively and illegally opposed organizing efforts. Other triggers of a non-compliance grade included (a) closed-shop practices that do not allow workers a free choice of who should represent them, and (b) workers not allowed to join organizations based on their work status and, in a few cases, blacklisting and dismissal of workers for such activities.

Effectively monitoring whether a worker truly has the freedom to associate and bargain collectively is also a challenge because there are many subtle methods employers might use to restrict workers’ rights to freely associate. While worker interviews are probably the most important tool for assessing compliance around this issue, it can only truly be tested during periods when workers are actively exercising this right,

which may not be when our auditors are present. It is our conclusion, and generally that of our industry colleagues, that we do not have a complete picture of the actual situation due to the challenge of discovering these practices through monitoring.

Our view is that this issue is closely linked to the lack of a history of constructive social dialogue and industrial relations in many of the countries where our products are made. Progress on this issue can only be sustained if workers and managers understand their rights, and local governments are willing to enforce their laws. But understanding isn’t the only issue. There are additional competencies needed for constructive social dialogue, e.g., conflict-resolution and negotiations skills, to name a few.

Freedom of Association	M-Audits with one or more instance of non-compliance
Freedom of association is prohibited by law (e.g., China, Vietnam)	10% - 25%
Freedom of association is prohibited due to exclusive union agreement	1% - 10%
Freedom of association is not provided where legal	1% - 10%

Our team has undertaken a range of activities to support our monitoring of this issue. We have an overall focus on education programs for Nike compliance staff as well as factory workers and managers. In addition, there are three components of our approach to strengthening industrial relations, both in countries where freedom of association is prohibited by law and where structural issues hinder workers’ ability to freely associate.

- **Grievance Systems:** We expect factories to have a grievance system and we monitor compliance against this standard. See section on harassment and abuse for more information about grievance systems.

- **Worker-Management Dialogue:** Another building block of freedom of association involves worker empowerment, including training workers to understand their rights and to engage in constructive dialogue with management. Training management to engage in dialogue with workers is another critical component of this process. In addition, we believe that workers and management have to practice skills that are important for industrial relations, regardless of whether workers choose to exercise their right to freely associate. We are working to facilitate the establishment of worker-management dialogues through standing ESH committees. Although we have put a lot of energy into this, we are still in the initial phase of implementation.

WORKERS IN CONTRACT FACTORIES

- **Direct Intervention:** Where worker rights are not adequately protected by others and we believe we have the ability to influence the outcome, we may directly intervene, often in consultation with external stakeholders with expertise on this topic.

Multi-stakeholder initiatives have been important in helping us explore different mechanisms for addressing the challenges surrounding freedom of association. Through the FLA and international trade union organizations, Nike also has addressed worker rights issues in factories in Mexico, the Dominican Republic, Thailand, Sri Lanka and Turkey, but to date there is not one systematic, global approach to this challenging compliance issue.

In Bangladesh, we worked with union and factory representatives to begin the first steps toward establishing protection for worker rights in export processing zones. The progress has been modest. Contract factory management sought court action to forestall the process, but then, under threat that the United States might withdraw trade privileges, reversed course and helped broker a new set of rules to allow workers to vote on representatives for a worker/management committee. There is little trust between factory and union management, which we intend to work to improve.

Bulgaria Apparel Project Partnership

As Nike began working with factories in Bulgaria, initial factory visits showed many examples of non-compliance with our code. This is not uncommon. As we looked at different factories, in part to avoid difficult compliance issues, we found that some of the problems were not limited to a small number of factories, but were endemic to Bulgaria.

Many of the issues were connected to freedom of association, and were rooted in the politics and culture of the former Soviet bloc. Some unions evoked either the style or image of unions under the prior regime. And factory owners, even many workers, placed little trust in them. Still, in a rapidly changing industrial economy, unions could play an important role. We helped create the Bulgaria Apparel Project Partnership to develop that role.

According to the charter agreed to in November 2003 by trade unions, suppliers, contract factories, government institutions, four brands (including Nike) and the Balkan Institute for Labor and Social policy, the partnership objectives are as follows:

- To encourage constructive dialogue between government, industry and the trade unions to help establish the Bulgarian apparel industry as a leader in corporate social responsibility
- To provide increased capacity building among workers, labor groups and employers and to build a better understanding of laws and standards that protect worker rights and their effects on such operational issues as cost, quality and profitability
- To integrate the state labor inspection machinery into the worker-employer dialog and familiarize the parties with a common set of references for corporate social performance. While many CR initiatives ignore the existing labor inspection machinery in place, this project will help strengthen it

The project may be important to Bulgaria. As the country seeks entrance into the European Union, its accession depends, in part, on its abilities to facilitate constructive social dialogue. European Funding (EU) funding for this project came primarily with this goal in mind.

In early discussions, the partnership focused on corporate responsibility issues alone – identifying compliance challenges, developing monitoring capacity, working with factories on remediation, etc. The companies found, however, that there would be greater benefit if the project addressed the fuller range of production issues, including price, quality and delivery.

Bulgaria Apparel Project Partnership has helped us understand that beyond the performance of factories, country-level competitiveness issues must be addressed if Bulgaria is to be considered a market leader in apparel. This shift in thinking – full integration of CR issues – mirrors our own shift at Nike.

Grievance Systems and Initiatives

In China, Nike has worked with local NGOs to develop reporting systems for employee grievances.

One such program, implemented in collaboration with the Ziao Chen Worker Hotline, started in July 2003. It began with an assessment of worker knowledge of Chinese labor law. Fifty workers were trained to be peer trainers on issues such as labor contracts, wages and leaves, health and safety, labor dispute resolution, insurance, and rights for female workers. Grievance communications systems were put into place and now include grievance boxes, a hotline, e-mail addresses and access to the labor union offices.

In May 2004, the factory workforce – more than 8,000 workers – elected 11 worker representatives from a slate of 15 candidates. These representatives will speak for workers on the Factory Grievance Committee (sitting with factory management and the state-sanctioned union). The committee is to resolve critical issues regarding workforce management and serve as a bridge between workers and management.

It is important to note that this is not a trade union; the committee sits under the factory management structure and will not engage in collective bargaining. But it is an important beginning and it will require ongoing development, education and empowerment.

A second program, implemented in collaboration with the Institute for Contemporary Observation, assisted with the Migrant Workers Grievance Program. ICO is also committed to developing worker's capacity in a variety of areas, from legal awareness, to occupational health and safety to reproductive health.

Harassment, Abuse and Grievance Systems

Of the different forms of harassment and abuse, verbal harassment is by far the most common form found by our monitoring team. Additionally, a series of worker interviews conducted by independent researchers for the Global Alliance (see sidebar) in Indonesia in 2000-2001 made Nike's compliance teams much more aware of the issues that young, predominantly female workers face when there is a climate of harassment, be

it physical, verbal or sexual. We have also learned that sexual harassment is very difficult to discover because of the sensitive nature of the issue, particularly in more socially conservative societies. For more information on the Global Alliance Study, see our FY01 CR Report at <http://www.nikeresponsibility.com/reports>.

Building the capacity of factory managers and workers to address the issue of sexual harassment is also a challenge.

WORKERS IN CONTRACT FACTORIES

Harassment and Abuse Grievance Systems	Audits with one or more instance of non-compliance
Workers do not trust the grievance process	25% - 50%
Workers report abusive treatment (verbal, physical, psychological, sexual)	25% - 50%
Confidential grievance system is not provided	25% - 50%

In Indonesia, we have implemented a pilot project in collaboration with a local NGO, Mitra Pembuan, specializing in women's rights and protection. The purpose of the pilot has been to explore how to tackle the issue of sexual harassment once discovered. While the post-project study is not yet complete, it has already taught us that even after intense training, sexual harassment is still not an easily understood concept and that training, by itself, is not sufficient to address this problem. We believe confidential grievance systems may be a more effective long-term solution because they allow workers the right to communicate incidents of harassment and abuse, and we have also concluded that our pilot effort, as implemented, does not represent a scaleable solution.

The sexual harassment grievance process has provided some key insights for factories, including the value of managing issues through a worker-management

grievance committee, the experience of working with the NGO community, and the realities of trying to sort through complex human interactions in a culture where harassment issues are not discussed in an open manner. As a result of their work in this area, a Nike contract factory was given a district award as the company providing the greatest boost to women's empowerment in 2004.

Our Code Leadership Standards instruct factories to institute a confidential grievance system – a practice that has not existed broadly in the industry. We believe our contract factories are beginning to understand the grievance system standard, as demonstrated by the growing number of factories with confidential grievance processes in place. Our auditors found that two-thirds of the contract factories audited now have such processes in place.

Worker Action

Our compliance team in China received phone calls from workers with complaints about conditions in factories. Through these phone calls, we learned about practices that are contrary to our Code of Conduct. This led us to discover the prevalence of double books or document falsification. While we did not track these calls in FY04, we plan to track this information for future reports.

Hours of Work

Nike's standard directs contract factories to limit the work week to 60 hours including overtime or comply with local laws if more stringent. In some

cases the Nike standard is more stringent than local labor law. Our auditors are trained to focus on hours of work during the factory's peak production period, to determine how the factory manages work hours

when it is busiest. In addition, our auditors bias their sampling to focus on workers who are most likely to be working overtime during the peak season such as final assembly and packaging workers.

Our studies indicate 10 or more triggers can lead to excessive hours of work, with responsibility somewhat equally divided. Buyers can be late to confirm styles, poor forecasting can drive orders up at the last minute, and order windows are often compressed to stay close to market trends. Factory managers may do a poor job of production planning or accept orders from multiple buyers well beyond their capacity to generate more revenue and keep buyers happy. High turnover rates may lead to low productivity, affecting production-planning targets. The nature of the industry itself creates overtime issues because seasonality drives peak production in a short window of time, and late delivery of materials delays the beginning of production runs.

In some cases, local authorities may contribute to the problem by granting exemptions that provide a *carte blanche* for factories to run beyond statutory limits.

As buyers like Nike set and try to enforce hour limits, some factories may hide their work practices by maintaining two or even three sets of books. They do this by coaching workers to mislead auditors about their work hours and by sending portions of production to unauthorized contractors where we have no oversight.

Overtime itself is probably the most consistent contributor to poor audit scores, because it can result in non-compliance in other areas: improper wages paid for overtime; switch hours that require workers to adjust their work weeks and shifts without proper notice, consultation, options or pay rates; harassment of workers who refuse to work extra hours; and health and safety issues tied to fatigue.

Overtime in China

Verité, an independent, nonprofit monitoring organization, reported in a 2004 study that excessive overtime – defined as work hours that exceed legal limits or the 60 hours per week standard in most corporate codes of conduct – is a widespread and persistent problem in the Chinese export industry. More than 93 percent of 142 Chinese factories audited by Verité for international brands during 2002 and 2003 employed excessive overtime.

To access the Verité report, please visit

<http://www.verite.org/Excessive%20Overtime%20in%20Chinese%20Factories.pdf>.

To the extent that we can put our orders in balance with the capacity of our factories, we believe that we can play a role in reducing some of the pressures that may lead to overtime abuse. It is important to note that this is only true for those factories where we have a high percentage of the production capacity because we cannot control the order flow from other buyers or monitor the acceptance of orders by our contract factories.

In many footwear factories, Nike is the sole buyer. In some cases, we are the only buyer the factory has ever had. Here, our relationship is strong, and our influence on management practices is comparatively enhanced. The same cannot be said of apparel and equipment factories, where our share of orders is lower, and violations of hours limits are more frequent.

WORKERS IN CONTRACT FACTORIES

Hours of Work	% of Audits with one or more instance of non-compliance
Work hours exceed Nike standard	50% - 100%
One day off in seven not provided	25% - 50%
Work hours exceed legal limit	25% - 50%
Overtime refusal results in penalty	10% - 25%

Until now, we have not had a systematic approach to address the issue of excess overtime beyond monitoring compliance with our standard. We can point to isolated examples when our production staff leveraged their orders to drive factory improvement.

For example, in Vietnam, starting in 1999, the Nike general manager directed all five contract footwear factories to prohibit Sunday work to help keep hours of work within the country's strict limits. When one factory was found to have allowed some Sunday work, the factory owner dismissed the manager. Our on-site

presence and M-Audits indicate those factories have largely met those standards in the years since.

Wages

Wages and hours of work are inextricably linked. Some suggest that workers are compelled to seek longer hours because their regular wages don't meet their basic needs. Others say workers want longer hours to earn more money to save because these are often short-term jobs. There is truth in both sides, and there are many other factors. The issue of wages as a policy question is addressed elsewhere in this report (see below).

Wages and Economic Development of Workers

Heated debates have raged about the level at which wages should be set for workers in apparel and footwear factories. Some worker advocates suggest that a living wage should be paid; various mechanisms are proposed for determining exactly what this wage would be in vastly different global regions. We do not support this approach.

Our view is linked to the understanding that wages are set, in most cases, by markets, and that markets tend to increase wages in those places where productivity is increasing. We look to ways of increasing productivity over the long term.

If wages are to be set by non-market mechanisms, we believe they should be set by those with the power to do so on a broad scale, including governments, industrial relations bodies (through collective bargaining) and employers' federations.

We monitor compliance with our Code of Conduct, which stipulates that workers in contract factories are paid the wages due to them. In regions where underpayment of wages is chronic, this can result in significant earnings growth in and of itself, particularly as it pertains to overtime wages.

We also focus on the matter of productivity. By this, we do not mean workers simply working harder. We are instead referring to the capacity of an individual or a community to produce goods or services that are highly valued in the open market. Our challenge is to provide opportunities for workers, mostly young women, to develop this capacity, with a focus on long-term economic advancement and increased earning capabilities. We would view it as a success if they could begin this track through their jobs in contract factories, which, for many, are their first job in the industrial economy. We have approached this challenge through significant investments in education and training. There is certainly room for innovation and improvement as we take these steps, and we expect to continuously search for new opportunities and approaches that will advance the economic status and quality of life of workers in our supply chain.

The impact of underpayment of workers, for reasons of inaccurate calculation or otherwise, is critical not only from a rights perspective but also because of the subsequent impact it can have on other working conditions, such as overtime, which is often sought to supplement inadequate wages.

Because wage laws, wage rates and record-keeping systems vary widely by country and even within countries, we look at wages from a number of perspectives. Monitoring compliance is further complicated by conflicting rules of compensation often with regard to eligibility for bonuses and incentives tied to individual and team productivity, allowances, deductions, skill premiums and so forth.

Factory documentation of compensation practices is another area where significant improvements are needed. Records, training and wage slip information were all found to be frequently sub-par against our standards, which require workers to receive a printed record of their wages, with clear itemization, in their own language. Our standard also requires that factories track hours worked with a timekeeping system and that workers receive documented training on how their compensation is determined.

There are at least three triggers causing incorrect payments to be made: poor pay management systems, outright manipulation and basic human error.

Wages	% of Audits with one or more instance of non-compliance
Overtime rate is less than legal or calculation is inaccurate	10% - 25%
Wage calculation is inaccurate	10% - 25%
Wage below legal minimum	25% - 50%

For the Nike compliance team, there is one question our auditors seek to answer: Are all workers paid what they were due for every hour worked? Our auditors have found that this is frequently not the case.

In FY03 and FY04, incorrect wage calculation, for regular and overtime hours, was a common finding by our M-Auditors. They also found a disturbing trend of non-compliance with minimum wage standards.

WORKERS IN CONTRACT FACTORIES

When we find payment below what is due to them, we direct the factory to pay back wages. Although we have not tracked this issue systematically across our supply chain, in FY04 a pilot initiative in our North Asia region led to more than \$720,000 returned to workers as back pay following the discovery of non-compliant compensation practices by our M-Audit team.

Sometimes the best learning and progress comes when one factory can demonstrate a better practice to another. Such a process occurred in Egypt, where, under the local labor law, a factory is allowed to deduct wages when a worker does not perform well, is tardy or otherwise does not meet the full expectations of the contract. The Nike standard is that wage deductions are not allowable, both to prevent management abuse that unfairly undercuts worker earnings, and because there are ample other means to manage people to better performance (or to manage chronic under-performance out of the factory). One Nike contractor had used fines as a management tool for some time. A second factory approached performance in precisely the opposite manner – using incentives, including bonuses, to manage better behavior. The Nike compliance team connected one factory with the other, and over a period of time the bonus approach has been implemented and fines eliminated.

Child Labor

Efforts by the international community, including governments and international institutions, to eradicate

child labor in the past 10 years has focused the world’s attention on this issue. And they have had some impact. For Nike’s own audit process, the most frequent non-compliance issues associated with child labor was improper age documentation. Because our age standards (18 for footwear, 16 for apparel and equipment, or local limits where they are more strict) are often higher than international or local age conventions, we find more issues of non-compliance with the Nike standard than non-compliance with local law.

Audits of 569 factories in FY03 and FY04 revealed a failure on the part of some factories to meet Nike’s age documentation standards. When compared to non-compliance in other issues and perhaps public perception, our auditors found very few individual issues in this category. The incidents were usually the result of careless human resource management practice or, occasionally, falsification of age documentation by the worker.

Over the course of FY03 and FY04, we found five workers who were hired below the local legal minimum age standard. All were within a few months of the legal limit when hired, and of those, several were of legal age at the time of our audit.

While we will continue to work hard to discover and prevent child labor from occurring, the low incidence rate suggests that this is not a common practice within our contract manufacturing base.

Age Standard	% of Audits with one or more instance of non-compliance
Worker age verification is inconsistent or not well-documented	10% - 25%
Worker age below Nike standard	1% - 10%
Age below legal minimum	Less than 1%

Looking Forward

Fiscal Year 2004 has proven to be a crossroads for us. Our monitoring systems have evolved to such an extent that we are now able to draw broad conclusions about non-compliance in the apparel, footwear and equipment industries.

We're also able to more clearly see that monitoring is a useful tool in two respects:

- As a mechanism for the discovery of issues
- As a mechanism for driving business integration and accountability, in our case through the balanced scorecard

What monitoring doesn't do is act as a remediation tool in and of itself. It also doesn't necessarily give a methodologically fair assessment of performance over time, because good monitors continually refine and deepen their discovery of issues on an ongoing basis.

What we have learned through our work in FY04 is that being able to comprehensively identify progress is a challenge. It is not that progress is non-existent. We have good case studies that demonstrate improvements, but we have not yet identified an appropriate metric for tracking the impacts of our interventions over time in a systematic, methodologically sound way.

In the absence of rigorous systems that align compliance performance with business performance, rewarding or sanctioning factories remains a challenge in a deeply competitive global environment.

Finally, and most importantly, we have concluded that monitoring on a factory-by-factory basis will not enable the great leap forward in working conditions across our industry. This will only come through multi-stakeholder partnerships enabled by full transparency of our industry supply chains.

These are important lessons. They guide us in our thinking about how we address the next generation of compliance in FY05 and beyond.

- We will continue to do monitoring because of the vital role it plays in feeding a grading system. However, we will shift resources away from Nike-led monitoring and towards business integration and multi-stakeholder collaboration on monitoring and remediation.
- We will actively, over the next years, focus on the following priority issues:
 - Freedom of association
 - Harassment, abuse and grievance procedures
 - Payment of wages
 - Hours of work
 - Environment, safety and health
- We will continue to drive efforts internally around the concept of a balanced scorecard, and seek to engage with business decision makers higher up in the production chain as part of our efforts to offer incentives for factory performance.
- We will refine our ability to measure progress and impact.
- We will engage in strategic multi-stakeholder initiatives that support efforts to encourage responsible competitiveness in the footwear, apparel and equipment industries.

Specific Plans for FY05-FY06

In FY05 and FY06, we plan to tackle the following:

Capacity Building and Remediation

- We plan to begin a shift to greater factory accountability, with factories trained to conduct self-assessments and a gradual growth in overall factory ownership of the compliance process.

WORKERS IN CONTRACT FACTORIES

- We plan to continue to explore scaleable solutions to help our contract factories build more robust confidential grievance systems, and will continue with our training programs to build awareness about harassment and abuse and worker-management communications.

Business Integration and Nike Compliance Processes

- We plan to work with research teams from the Sloan School of Management at the Massachusetts Institute of Technology (MIT), and to examine a range of questions around the business drivers and outcomes. We hope to gain insights about the whole of the business process, with the goal of helping both Nike and contract factories better manage production flows and the factories manage hours of work. In addition, we are currently working with external parties to look at some of these issues more deeply in the areas of environment, safety and health.
- We plan to work with production managers to focus their leverage and our compliance team's assistance on factory remediation to drive improvements among D-rated factories.
- We plan to launch an internal task force to examine the entire business cycle as it relates to overtime. This will include exploring the links between the flow of orders and production capacity within those factories where we have greater leverage. It will also seek to identify those issues that can be addressed internally and those issues that are more effectively addressed through industry collaboration and multi-stakeholder initiatives.
- We plan to continue to monitor compliance with our wage standard and to explore mechanisms to strengthen basic human resource management practices among our contract factories.

- We plan to have more robust data documenting the length of time factories remain within the more critical ratings categories.

- We plan to work closely with the business to identify changes in the source base that might lead to impacts on workers and, where we identify those, consider activating the factory exit process. Externally, we will continue to engage with stakeholders through the MFA Forum and, where appropriate, support local efforts to mitigate impacts that might affect Nike contract workers.

Multi-Stakeholder Partnerships

- We plan to work with our industry counterparts to encourage broader disclosure of supply chains, and we plan to seek out and support effective coalitions of companies, trade unions, NGOs, multi-lateral agencies and governments to raise standards for our supply chain and our industry.
- We plan to identify and participate in programs designed to raise the overall performance in a particular country's footwear, apparel or equipment industries. We support the type of programs currently in development by the World Bank in a number of key Nike source countries, including Cambodia, Vietnam and Indonesia. We will continue to participate in the MFA Forum as part of our work around the impacts of this trade agreement.
- We plan to look for broader-based coalitions to address endemic issues within specific countries or regions, such as working to facilitate parallel means of representation in China.

Two years ago, Nike set out on a five-year journey to make the company an Employer of Choice. We said diversity could be a competitive advantage. We said we wanted to be recognized as one of the best places to work. While we have received feedback from our employees that overall satisfaction levels are high, we also know there are many areas where we can improve.

Scope

This section covers employee-related issues for those working in Nike, Inc. owned and operated facilities, including subsidiaries where specified. Due to transitions in our global data collections systems for employees, we have not reported data on our global employee base. Select data is provided on U.S. employees.

STRATEGY

The connection between diversity and business results is at the core of Nike's global diversity strategy. Our strategy focuses on diversity in the workforce, workplace and marketplace. Nike employees believe that diversity pumps creativity and innovation into our brand, helps us recruit the most talented workers and leaders, and brings us closer to our culturally attuned consumers. While diversity means different things to different cultures, there is a constant; a highly inclusive company culture is one that is open and welcoming to all, regardless of race, gender, ethnicity, sexual orientation or physical capabilities.

ISSUES AND IMPACTS

In FY04, Nike conducted a survey of its employees globally to determine how Nike can more fully capitalize on the talents of all employees. The confidential Web- and paper-based survey was translated into 10 languages and coordinated by

a third party. The survey was designed to uncover commonalities, as well as differences, within Nike's global workforce.

The survey assessed employee attitudes and perceptions, particularly related to the following topics:

- Work environment
- Career advancement
- Diversity and inclusion
- Employee recommendations

We received 9,044 responses to the survey and interviewed 75 current and former Nike leaders from around the globe. The Web-based survey response rate was 80.6 percent. The paper-based survey response rate was 30.2 percent. The overall useable survey response rate was 51 percent. The survey was given to all employees except Nike Retail and the subsidiaries.

EMPLOYEES AND DIVERSITY

Among the survey's highlights were the following:

- Employees join Nike for opportunities and for personal development and advancement.
- Our employees are impassioned and hard working. They often do not seek to separate who they are from what they do. Nike requires an intense commitment from them, and they most often willingly respond to this.
- Nike is a culture driven by relationships. Being a team player emerged as the most important factor for success.
- Nike's systems and processes have not grown sufficiently to support the needs of a global company. Employees cited the lack of infrastructure for people development systems as a barrier to success.
- Employees often spoke about the increasing visibility given to Nike's current diversity efforts, but still feel there is more to do.
- Employees have moved well beyond a compliance model in conceptualizing the business case for diversity. They believe that leveraging Nike's diverse perspectives will lead to increased creativity and innovation.

The survey indicated that most employees are pleased to work for Nike, and that satisfaction and enthusiasm are shared across groups of employees. Still, Nike employees had recommendations for changes, focused in these four areas:

- Management education
- Career development
- Flexibility/work life effectiveness
- Management accountability

The results of the employee survey were communicated to Nike employees throughout the world. Staff members from the Office of Global Diversity conducted more than 100 presentations in 16 countries.

Work teams were established to address the employee recommendations from the survey. Each work team

consisted of 10 to 12 members and was co-led by a human resources leader and a leader from one of Nike's business units. The work teams conducted external research on best practices and recommended strategies to implement change to maximize workforce value.

BUSINESS INTEGRATION

Nike's corporate responsibility board committee is responsible for providing oversight on policies and activities related to the issue of diversity.

In FY04, we made significant changes in how we manage for diversity.

- Our **Office of Global Diversity**, established in FY04 with a staff of four, is the catalyst for developing fair and consistent diversity practices in all areas of our business. It is responsible for global strategy and policy development; leadership coaching and development; assessment and measurement; and communications and linking with other units in the business, including supplier diversity, staffing, corporate responsibility and community affairs.
- Our **Global Diversity Executive Council**, also established in FY04 and co-chaired by Nike Brand Presidents Mark Parker and Charlie Denson, provides oversight and direction to the Office of Global Diversity. The responsibilities of the 14-member council include reviewing policies and strategies, defining roles of leadership and their impact on managing global diversity, articulating global diversity agenda that everyone can understand and get excited about, and driving accountability throughout the organization.
- The **Global Women's Leadership Council** was established to promote and support the career advancement of women within our organization; it is focused on advocacy, building connections, catalyzing action and measuring results. Advisory teams, involving 155 men and women from across Nike, were created to support the Council.

Nike has several programs and activities that support diversity throughout the company.

Diversity workshops

We offer several management training courses that explore the value of, and strategies for, workplace diversity. In FY04, more than 2,000 Nike managers

and employees in the United States attended at least one of our workshops. While participation in these workshops is not mandatory, attendance rates have been strong. Business units have requested additional workshop sessions to accommodate their employees.

Workshop Title	Workshop Description	Target Audience
The Potential Is Yours	This workshop presents the basic concepts of workplace diversity. It emphasizes employee interaction and effectiveness in three areas: personal, interpersonal and organizational.	Open to all U.S. employees.
Maximizing Diversity and Inclusion	This workshop is designed to increase awareness about diversity and inclusion in the workplace. It provides managers with practical skills to manage a diverse workforce through interactive learning.	Open to all U.S. managers.
Diversity Workshop	This workshop provides in-depth education and awareness of the primary dimensions of diversity. It is formatted to emphasize group discussion and activity.	Open to all senior-level managers.
Competency-Based Selection	This workshop provides an understanding of the fundamentals of an employee selection process, how to design better interviews and make better decisions.	Open to all managers and individual contributors participating in the selection process.
Managing to Win: Fair and Legal Employment Practices	This workshop is designed to translate complex legal issues into information U.S. managers can use on an everyday basis. Participants are taught how to apply fair and legal employment practices in a broad range of workplace situations through interactive learning.	Open to all U.S. managers.
Managing to Win Refresher	This workshop provides a review of the principles of civil treatment and an update on Nike policy and legal trends. Participants must have attended the Managing To Win: Fair and Legal Employment Practices.	Open to all U.S. managers.
Corrective Action	This workshop provides managers with the tools to redirect substandard performance using a positive process with the goal of achieving desired performance, not termination.	Open to all managers.
Playing Fair, Harassment – Zero Tolerance*	This workshop reinforces Nike's policy of prohibiting harassment, ways to prevent harassment and Nike employees' complaint process.	Open to all employees.
Let's Talk About It: Nike's Grievance Process	This workshop provides employees with information and resources to help resolve issues.	Open to all employees.

EMPLOYEES AND DIVERSITY

Employee Networks

In the United States, six employee networks focus attention on important communities within Nike. The intended role of the networks is to foster professional development, enhance work performance, identify mentors, assist in recruiting diverse professionals, develop increased community interaction, and encourage improved teamwork and interaction within and across work groups. The six Nike networks are as follows:

- African-American (established pre-1996)
- Asia Pacific (established 1994)
- Disabled Employees & Friends (established 2000)
- Gay, Lesbian, Bisexual, Transgender & Friends (established 1998)
- Latino & Friends (established 1993)
- Native American (established 1998)

Examples of network achievements in FY04 include: youth leadership training; sponsorships of physical activity programs for minority youth and community members at Nike's World Headquarter facilities; regional and national speakers sharing personal and minority community challenges and achievements; and cultural heritage events.

Diversity Committees

- Memphis, Tennessee, Distribution Centers established a Multi-Cultural Awareness Committee (M.A.C.) in 1998
- Wilsonville, Oregon, Distribution Center established the Wilsonville Diversity Committee pre-1998
- USA Region Leadership Team began a diversity steering committee
- USA Retail began a diversity steering committee with representation from all levels within the organization

Regional Diversity Efforts

- Europe, Middle East and Africa region held its first women's symposium, began a diversity task force, required that 50 percent of all candidates for leadership positions be women and implemented flextime scheduling at Nike European Headquarters (EHQ).

- The Americas and Asia Pacific held career networking events for women in their regions.

EEO Data /Affirmative Action Plans

In the United States, Nike leverages its affirmative action plans to develop action-oriented plans to improve our effectiveness in attracting, retaining and promoting a diverse workforce. In FY04, Nike successfully partnered with the Office of Federal Contractor Compliance Programs (OFCCP) to restructure, where applicable, the plans to align with our business functions or divisions. The Functional Affirmative Action Plans provide a clear direction for Nike business leaders in their respective divisions.

Hiring, Promotion and Retention Data

Nike's human resources (HR) information systems posed limitations in our ability to capture and report data on a global scale. A multi-year, global HR information systems strategy is currently being implemented, with the goal of project completion in FY06. As part of the overall global HR strategy, a work team will be established in FY05 to focus on a Global HR Scorecard. In FY05 - FY06, the team will work to define the purpose and goals, audience and accountability, metrics, measurements and design, ownership and maintenance processes. Global consistency in reporting relevant key metrics is one of the desired outcomes.

Supplier Diversity

Our supplier diversity program supports U.S. supply purchases from minorities, women and physically challenged business owners. Nike currently spends approximately \$1.9 billion annually on indirect goods and services, of which \$910 million is classified as addressable spend (spend the procurement department is able to influence). In FY04, Nike spent approximately \$33 million with minority or women-owned business enterprises (MWBE), or 3.7 percent of our total addressable spend. The Supplier Diversity

Program has been running since 1998 and has taken great steps forward, however we will soon be in a position to drive significant change as we appoint a new Supplier Diversity Program manager. Once in place, the program manager will develop a robust operational backbone in the program. Nike works with several national and regional partners, including the National Minority Supplier Diversity Council, the Abilities Fund and the Oregon Association of Minority Entrepreneurs to help expand the MWBE supplier base.

Within the next 12 to 24 months we expect to see significant progress in the area of supplier diversity. The following are the main areas of focus for the program manager:

- Develop a set of metrics that track and articulate year-on-year growth for MWBE expenditure.
- Promote timely introduction of suitably qualified vendors within the bidding cycle and further ensure that we have a minimum representation of 25 percent MWBEs in each solicitation of bids that Nike's sourcing team distributes.
- Work to convert 10-15 percent of the participating MWBEs into live contracted vendors.
- Develop and deliver an internal training program aimed at those buyers that are not currently employed within the procurement department, and promote inclusion of suitably qualified MWBE vendors within their bidding cycle.
- Include all details for new vendors correctly in the master log; such detail will include but not be limited to classification of MWBE status and certification verification.
- Issue timely reports concerning the program and expenditure that can be attributed toward it.

Compensation and Benefits

Our benefits rank among the 90th percentile in the United States when compared to our elite peers.

Benefits include performance sharing bonus plan; a profit-sharing plan; a discounted stock purchase program that allows employees to purchase stock at a 15-percent discount; a multi-level health care plan; permanent partner health (since 1994) and adoption benefits; supplemental disability and optional long-term care and group life insurance; a retirement savings plan; and tuition assistance.

Fitness facilities and programs are provided at many locations, with drop-in day care at select facilities for employees and family members.

The Employee Assistance Program (EAP) and LifeCare® provide counseling and referrals on a wide variety of topics to help employees manage their lives and relationships.

Sabbaticals of five weeks are provided as a reward for employees who have worked for the company for 10 years. Employees are eligible for subsequent sabbaticals every five years thereafter.

Other benefits can include subsidized mass transit; Nike product at wholesale prices for employees and their families; limited full-time pre-school and day care at our WHQ; alternative transportation incentives (monthly and quarterly prizes for employees who walk, bus, run, ride, carpool or shuttle to work); and discounts with business partners, local and national retailers, service providers and lending institutions.

EMPLOYEES AND DIVERSITY

PERFORMANCE

Diversity

The following chart reflects racial and gender diversity at Nike.

Nike Board of Directors and Management				
	Board Members		Executives and Senior Managers	
	#	%	#	%
Women	2	20%	93	27%
Men	8	80%	257	73%
People of Color	1	10%	49	14%
Total	10		350	

**U.S. Information only*
– People of color based on the U.S. Equal Employment Opportunity Commission’s definition of minorities.
– This data represents active U.S. employees as of 5/31/04 (excluding subsidiaries).

Employees

U.S. Breakdown by Gender/Race			
U.S. Region	Male	Female	People of Color
Employee Count	6,239	5,731	4,532
Percentage	52%	48%	38%
EMEA Region	Male	Female	Total
Employee Count	2,851	3,189	6,040
Percentage	47%	53%	

• Data not currently available for all Nike employees globally by gender.
• Data varies slightly from numbers reported in company profile due to differences in data-tracking systems.

Trade Union Relationships

Nike employees at several locations are represented by independent trade unions. As is true of our Code of Conduct for contract manufacturers, Nike supports the right of freedom of association and collective bargaining within our owned and operated facilities. These include employees in Canada, Italy and Laakdal in Belgium. In Europe we have a European Works Council, which has elected representatives from each of the National Works Councils who may or may not be members of a trade union.

We do not keep information on the number of Nike employees who are members of unions.

During FY04, three different unions represented employees at Bauer Nike Hockey’s Canadian facilities producing Bauer Nike Hockey equipment. Bauer Nike Hockey is a subsidiary of Nike, Inc. It is unique among brands within Nike, Inc. because many of its products have been made in facilities owned by the company.

In FY04, Bauer Nike Hockey announced the closure of two facilities based in Canada. The Hespeler facility in Cambridge had produced wood hockey sticks, and production was shifted to a different Canadian facility making composite sticks. Employees at the new facility are not represented by a trade union. This production shift resulted from the decline in market demand for wood sticks, although some wood sticks continue to be manufactured for Bauer Nike Hockey by a group comprised of the former facility manager and a small number of former employees using the former Hespeler facility.

The second facility to be closed was the Eastgate facility, which manufactured goalie protective equipment. Much of this production was moved to another Canadian manufacturer whose employees are not represented by a union. At a third facility, St. Jerome, production was reduced, also resulting in a loss of jobs.

The unions urged Bauer Nike Hockey to reconsider the closures, but to remain competitive in the hockey market, Bauer could not change the decision.

The Hespeler facility was represented by the Industrial, Wood and Allied Workers of Canada (IWA), and Eastgate was represented by the Glass, Molders, Pottery, Plastics & Allied Workers International Union (GMP). Plant closure agreements were in place as part of the collective agreement (labor contract). The collective agreement with the IWA, however, was open, and in negotiation we enhanced the severance payments. At our facility in St. Jerome, provisions in the collective agreement regarding plant closure or layoffs provided for severance benefits to employees with five or more years of service. Nike Bauer Hockey provided outplacement services to its Eastgate and Hespeler employees in excess of what was required in the plant closure agreement.

The GMP has filed one grievance against Bauer Nike Hockey over the closure of the Eastgate facility; as of December 2004, there was no resolution to that grievance.

Awards and Recognition

In 2002, 2003 and 2004, Nike achieved 100 percent ratings on the Human Rights Campaign's Corporate Equality Index Survey (<http://www.hrc.org>).

Nike was the 2004 U.S. Western Region Employer of Choice by the Minority Corporate Counsel Association. The award spotlights industry leaders who have a commitment to, and success at, creating and maintaining an inclusive corporate legal department (<http://www.mcca.com>).

Plans for FY05 and Beyond

Nike has been active in its commitment to diversity for many years, but like many aspects of our business, as we have grown and matured in recent years we have realized the importance of putting formal structures and systems in place. We are now building the infrastructure to tackle diversity, starting by understanding our issues and impacts through employee surveys and external advice. An important part of knowing our impacts is having access to the data to assess this question. By FY06, our goal is to have complete coverage of our global employee base through a uniform data collection system. This will allow us to finalize our strategy, identify appropriate metrics and set the targets that we need to improve and that our stakeholders,

internal and external, need to judge our performance.

Over the next three years, Nike plans to develop and refine our goals, metrics, targets and accountability measures around the following priority areas.

Priorities were identified through employee feedback provided through the employee survey (Management Education; Career Development; Flexibility/Work Life Effectiveness; Management Accountability), external benchmarking and independent expert guidance.

Workforce and workplace diversity priorities include the following:

- Representation of senior management
- Organization and leadership development
- Career development
- Introduce formal mentor program
- Inclusion of diversity goals in all business plans
- Management accountability for diversity goals
- Improve effectiveness of recruitment strategies
- Expand work/life effectiveness programs
- Effective internal communications and transparency

Marketplace diversity priorities include the following:

- Supplier diversity
- Stakeholder engagement and partnership
- "Best of" lists
- Diversity goals

Like our efforts to improve conditions for workers in our contract factories, Nike's Environmental Management System continues to evolve. Our goals and data collection systems have been refined. Our strategy now focuses on sustainable product innovation – linking the work to the products that drive Nike's business. We continue to find new partners, both within our supply chains and the public sector, because we view environmental progress as a shared responsibility, particularly within our supply chain. We are pleased with this development. We're beginning to explore mechanisms for discussing these issues with consumers.

What has not changed is our long-standing commitment to reduce our environmental impacts and move in the direction of sustainability.

STRATEGY

In our FY01 report, we articulated a set of long-term goals related to the environmental aspects of our products, including zero toxics, zero waste and 100 percent closed loops. Over the last three years, we tested the relevance of those goals within the business and with external stakeholders, and reframed them based on feedback and practical experience. In FY03, an assessment of our impacts and activities, conducted by The Natural Step, confirmed the following:

- Most impacts were upstream (manufacturing and production) and downstream (end of product life) of our owned operations.
- Existing goals and initiatives covered a wide range of flows and impacts.
- There was limited integration and alignment of efforts with key business owners and practitioners.
- The business case for action in many areas was unclear.

This review led to us to give a higher priority and a renewed emphasis to sustainable products, because

products are the core of our business. Our single unifying goal in FY04 and beyond is to create innovative and sustainable products. With this integrated, business-relevant approach, we ultimately will be able to focus our efforts against the two long-term goals of waste and toxics elimination.

This goal of innovative and sustainable products has applications beyond consumer products; it can guide our operations and those of our suppliers, as environmental impacts occur at every stage in the life cycle of Nike products. They begin when raw materials are first cultivated, extracted and processed; continue when a product is manufactured and distributed; and extend to use, care and final disposal by consumers. Nike has varying degrees of control and influence at these different stages which in turn affects our ability to address effects. Product design is mostly under our direct control, as are distribution and some retail (see *Company Profile* section of the FY04 10-K). Materials supply, manufacturing and transportation are contracted out.



The key focus areas for managing environmental impacts throughout the product life cycle are as follows:

Promote compliance with environmental standards set by others or by Nike.

- Continue to help ensure that our tool, the Restricted Substances List, is used and implemented across all our apparel, footwear and equipment products
- Continue to build the infrastructure for managing environment, safety and health in our owned operations
- Complete our program to eliminate all remaining greenhouse gases from our footwear
- Reduce the use of water and improve wastewater management standards across our supply base
- Commercialize affordable non-PVC alternatives for screenprint inks, heat transfers and dimension welds

Eliminate waste and toxics across our product lifecycle.

- Focus on solid waste elimination from footwear manufacturing
- Continue to work on the reduction of CO₂ emissions across the business
- Build on efforts to eliminate volatile organic compounds from footwear manufacturing and extend lessons to other areas of product manufacturing

Build our corporate ability to use four key sustainable material platforms:

- **Organic:** Organic is used to describe an agricultural method in which crops are grown without the use of synthetic chemical pesticides, fertilizers or defoliants. Example: Organic cotton.
- **Chemically Optimized:** Materials determined to contain a significantly lower amount of chemicals deemed to be of concern based on Nike's toxic chemical assessment. The assessment reaches well beyond legal requirements for product chemistry and seeks to promote the development of environmentally preferred chemistry. Example: Environmentally preferred rubber.
- **Regenerated:** Reprocessed materials or products that can be converted to new products. Example: Closed loop materials.
- **Renewable:** A (cultivated) plant-based raw material resource that can be used to manufacture natural or bio-based textile fibers and polymers. Example: Polylactic acid (PLA).

Packing and shipping

- Reduce the environmental footprint of packaging and shipping of our products and bring efficiencies to the business

Waste as a business opportunity

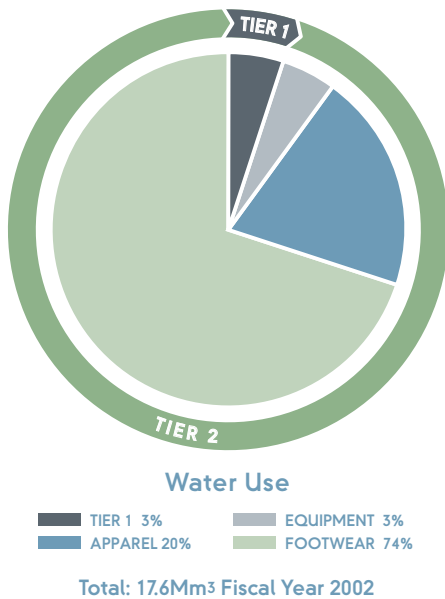
- Implement innovative programs that turn waste into a business opportunity. For example, Reuse-A-Shoe

IMPACTS AND ISSUES

In FY01, we reported on a number of areas we had identified as significant, including PVC phase-out, organic solvent elimination, organic cotton use and SF₆ phase-out. Since then, we have examined other impacts we knew needed to be addressed more systematically; these include our environmental footprint for waste, water, energy and CO₂ emissions across Tier 1 (Nike operated facilities) and Tier 2 (contract factories) operations.

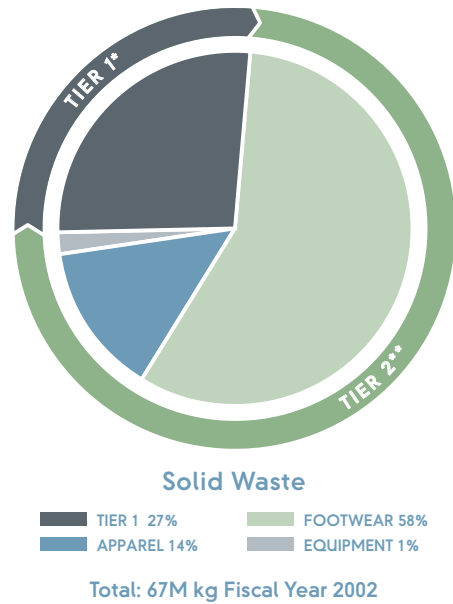
ENVIRONMENT

The charts below, based on 2002 collected data, show the **relative** proportion of the footprint for water, solid waste, and energy for Tier 1 and Tier 2. They provide a snapshot in time and a starting place for prioritizing and allocating resources. The Performance section contains key performance indicators for those impacts that we will measure and track over time.



Ninety percent of water usage in Tier 2 (footwear factories) is for domestic purposes (drinking and sewage). Nike's efforts with respect to apparel, however, are focused on Tier 3 (material suppliers) where most of the water-related impacts occur. For more information, please refer to the water section of this report. Note that most of footwear's water-related impacts will also occur in Tier 3 materials (leather tanning/processing, synthetic leather).

Source: Data was collected through a representative survey of Tier 1 and Tier 2 operations. Engineering estimates were then used to scale up the data to represent the full footprint.

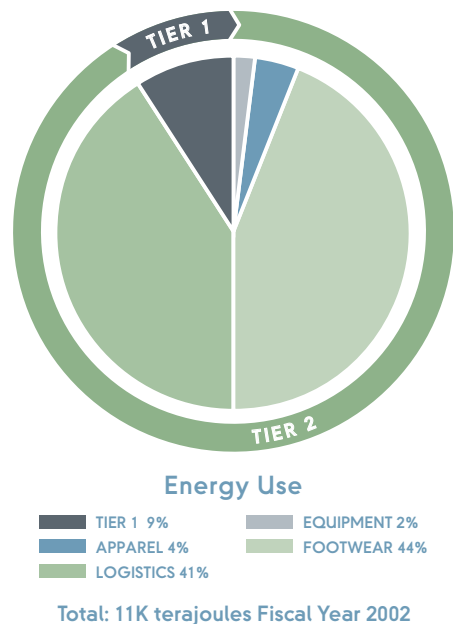


Engineering estimates were made of the proportion of solid waste generated that was recycled.

*81% Tier 1 waste recycled

**48% Tier 2 footwear waste recycled

Source: Data was collected through a representative survey of Tier 1 and Tier 2 operations. Engineering estimates were then used to scale up the data to represent the full footprint.



Source: Data was collected through a representative survey of Tier 1 and Tier 2 operations. Engineering estimates were then used to scale up the data to represent the full footprint.

To help us understand where we have the greatest impacts – and therefore where we need to focus our priorities – the following matrix identifies all our initiatives and the related product life cycle aspects.

Life Cycle Matrix of Environmental Initiatives

		Life Cycle Stage					
Focus Area	INITIATIVE	PRODUCT CREATION	MATERIALS	MANUFACTURING PROCESSES	DELIVERY PACKAGING & LOGISTICS	CONSUMER END OF LIFE	CORPORATE OPERATIONS
	COMPLIANCE	RESTRICTED SUBSTANCE LIST PROGRAM	■	■	■	■	■
		ESH PROGRAMS	■	■	■ *	■	■
		SF ₆ & PFP PHASE-OUT	■	■	■	■	■
		WATER QUALITY	■	■	■	■	■
		WATER CONSERVATION	■	■	■	■	■
		PVC PHASE-OUT	■	■	■	■	■
	ELIMINATE WASTE AND TOXICS	SOLID WASTE ELIMINATION	■	■	■	■	■
		CO ₂ EMISSIONS REDUCTION	■	■	■	■	■
		HAZARDOUS WASTE ELIMINATION	■	■	■	■	■
		VOC REDUCTION	■	■	■	■	■
	SUSTAINABLE MATERIAL PLATFORMS	ORGANIC COTTON	■	■	■	■	■
		ENVIRONMENTALLY PREFERABLE RUBBER	■	■	■	■	■
		REGENERATED CONTENT PROGRAM	■	■	■	■	■
		RENEWABLE CONTENT PROGRAM	■	■	■	■	■
	PACKAGING & SHIPPING	PACKAGING	■	■	■	■	■
	WASTE AS A BUSINESS OPPORTUNITY	RECOVERED PRODUCT	■	■	■	■	■

■ IMPLEMENTED PROGRAM
■ FUTURE OPPORTUNITY
■ (NOT MATERIAL): ASSESSED AS LOW IMPACT/ SIGNIFICANCE, WELL BEYOND OUR ABILITY TO INFLUENCE TODAY, OR IMPACT DOES NOT ARISE AT THIS STAGE OF THE LIFE CYCLE

*SEE LABOR

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Business Integration

Embedding sustainability teams within Nike's product engines (apparel, footwear and equipment) is fundamental to our strategy of pursuing sustainable product innovation. These dedicated teams work with colleagues to weave environmental programs into the heart of the business. Equally important is the sharing of best practices and knowledge across the different product engine sustainability teams. A good example of this is our solid waste elimination program; launched and tested in footwear, it is now helping us design a solid waste elimination plan within our apparel business.

Demonstrating the added value of sustainable product innovation to our business model and, ultimately, to the consumer, is crucial to our long-term success within this field. We have pockets of success, but must continue to build the structure, competencies and new business models if we're to systematically weave sustainability into our product lines.

The reality is that today we are investing in sustainable product without seeing the return on our investment. Consumers may not yet understand sustainability as a purchasing incentive, and we are not yet promoting many of our efforts to consumers. If the investment in a sustainable material drives up the price of the product, consumers may not be willing to pay for the difference.

One important way to drive down the cost of the initial investment – in R&D, raw materials or production costs – is to work with others. Partnerships can help us take programs to scale where higher volumes can help us gain better prices for materials or services. Partnerships can also help us create new markets, a vital step for a strategy based in product innovation.

Multi-Stakeholder Partnerships

As noted elsewhere in this section, we are increasingly working in partnership with others – our contract manufacturers, NGOs, governments, academic and scientific communities or other business community members. Our effort to build the organic cotton industry is a good example of how important partnership approaches are to our ability to deliver against our objectives. Without working collaboratively with others to build the supply, we could not continuously increase our use of organic cotton. Our environmental partners include the following:

World Wildlife Fund: Climate Savers Initiative

Under the Climate Savers agreement, Nike became the first footwear and apparel company to commit to an absolute CO₂ reduction target, and is one of the eight companies that have joined the World Wildlife Fund's (WWF's) Climate Savers initiative. In the Climate Savers initiative, WWF and the Center for Energy and Climate Solutions work with companies like IBM, Johnson & Johnson and Polaroid to develop practical, cost-effective strategies that reduce CO₂ emissions and achieve energy efficiency goals.

Business for Social Responsibility (BSR)

BSR Working Group: Clean Cargo

The Clean Cargo Working Group is comprised of leading multinational manufacturers and retailers (shippers) and carriers, formed in 2001 to promote sustainable product transportation by sea and land.

BSR Working Group: RSL

This is a working group of apparel brands and retailers focused on restricted substances. The intent was to understand legislation and trends around restricted substances as they apply to finished apparel products. (Participants include Nike, Levi's, Gap, H&M, REI, LL Bean, Kellwood, Nordstrom, Timberland and Patagonia. Group headed by BSR.)

BSR Working Group: Water

A working group of apparel brands and retailers focused on process wastewater issues at the vertical factories, laundries and textile mills. The goal is to update current guidelines and develop strategies for implementation and monitoring.

National Recycling Coalition (NRC)

NRC works with thousands of public, private and nonprofit sector organizations across the nation to maximize recycling. NRC members participating in the Reuse-A-Shoe program collect post-consumer athletic shoes of any brand through various recycling programs, allowing them to divert a new and different material from the waste stream.

Phylmar Working Group – RSL

This working group of apparel brands and retailers focuses on restricted substance lists, education tools and supplier communications as they apply to the contents of final product. When possible, best practices and tools will be shared within the working group. (Participants include Nike, Levi's, Adidas, Puma, Gap, Marks & Spencer, C&A. Group headed by Phylmar Consulting.)

Green Blue Sustainable Packaging Coalition

This working group of packaging and environmental professionals, ranging along the value chain from paper and resin manufacturers to consumer product companies and retailers, provides a forum for identifying opportunities for sustainable packaging. Member companies include Biocorp, Cargill Dow, Coca Cola Company, Design & Source Productions, Dow Chemical, Dupont Soy Polymers, Environmental Packaging International, Estee Lauder/Aveda, EvCo Research, Johnson & Johnson, Kraft, MeadWestvaco, Metabolix, Nike, Pepsi Co., Priority Metrics Group, RSVP Packaging, Starbucks, Target and Unilever.

Metafore

The goal of the Metafore Paper Working group is to develop a more predictable and affordable supply of environmentally preferable paper through the development and adoption of a new paper scorecard that ranks the various issues through the paper supply chain. Member companies include Starbucks, Time Inc., Cenveo, Nike, Norm Thompson, Staples, Toyota, Hewlett Packard, Bank of America, McDonalds and FedEx-Kinkos.

Organic Exchange

The Organic Exchange is a nonprofit business organization focused on facilitating the growth of a global organic cotton industry. The long-term goal of the Organic Exchange is to promote building a global organic cotton industry that satisfies 10 percent of the world's demand for cotton fiber within the next 10 years. The Organic Exchange will do this by bringing together companies in all parts of the organic cotton value chain; providing a forum for identifying and addressing barriers to industry growth; supporting the development of information, business networks and new business models, processes and metrics needed to facilitate industry growth; and facilitating business-to-business transactions. A Nike representative serves on the board of directors for the Organic Exchange.

Organic Trade Association

The OTA is a business association representing all sectors of the organic industry in the United States, Canada and Mexico. Its more than 1,200 members include growers, certifiers, brokers, retailers, importers, exporters and others. OTA's mission is to encourage global sustainability by promoting and protecting the growth of diverse organic trade. A sector group, the Organic Fiber Council (OFC), was formed in 1997 to address topics of interest to businesses within the organic agricultural industries, including cotton, wool, hemp and flax. A Nike representative serves on the OFC steering committee.

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Society of Organizational Learning (SoL)

Sustainability Consortium

This consortium of companies is committed to accelerating the education needed to achieve a truly sustainable economy. The consortium utilizes the disciplines of systems thinking and organizational learning to explore and address the challenges of remaining profitable while nurturing the natural systems and the communities in which we do business. Member companies include BP, Shell, Ford Motor Company, Visteon, Harley Davidson, Green Mountain Coffee Roasters, International Finance Corporation (IFC), Nike, DTE Energy, Plug Power, Pratt & Whitney-United Technologies Corporation, Schlumberger, Unilever and The Coca-Cola Company.

SoL: Corrugated Working Group

SoL is a working group of packaging and environmental professionals developing a map and matrix of the current markets, flows of materials and potential sustainability issues for corrugated packaging materials. This data will be utilized to develop strategies and steps for improvement. Member companies include Nike, Estee Lauder/Aveda, Harley Davidson, Hewlett Packard and Unilever.

SoL: Leather Working Group

A working group focused on developing an understanding of the sustainability issues within the leather industry and generating solutions to more sustainable leather.

Product Sustainability Round Table

This is a consortium of companies that provides members with opportunities to benchmark product-related environmental programs; to keep informed about emerging tools, practices and policy developments; and to refine their understanding of the business benefits associated with sustainability. The membership of each roundtable represents a broad spectrum of organizations throughout the industrial

supply chain, enabling the exploration of practical approaches to implementing sustainable strategies. Member companies include Alcoa, Armstrong, ArvinMeritor, BASF, Black and Decker, Boeing, General Motors, JohnsonDiversity, New York City Transit, Nike, Rio Tinto Borax, SC Johnson, United Technologies, ABB and Unilever.

PERFORMANCE

This section of the environmental overview is organized under the five areas of focus in promoting compliance with environmental standards outlined in the Strategy section (page 56).

COMPLIANCE

Restricted Substances Lists

Nike has implemented restricted substances lists (RSL) for finished product, manufacturing (MRSL) and packaging (PRSL). The RSLs are global lists of substances restricted or prohibited in Nike brand footwear, apparel and equipment. We are working to ensure that restricted substances are not used in Nike products. The lists are predominantly based on the most stringent worldwide legislation, with an eye to legislation trends and stakeholder concerns. The intent of the RSL portfolio is to protect the consumer, the worker, the environment and the brand, and ensure the safe importation of Nike product to any market in the world.

The next phase of Nike's chemical/product stewardship will involve a broader look at toxics. This phase will take Nike above and beyond regulatory compliance; it starts us on the path of improving our products by proactively targeting, removing or replacing chemicals that, while not legislated as illegal, fit the scientific definition of toxic. This is a long-term project that will require us to work closely with the scientific community, stakeholders, our supply chain and other wholesalers and retailers. We've taken voluntary steps beyond

regulatory compliance in the past; what sets this apart is that the approach is far more comprehensive.

Environment, Safety and Health in Our Owned Facilities

Nike seeks to protect and enhance the brand and the company by being a global leader in environment, safety and health (ESH) management. Linking the ESH mission to the larger company mission is an important step; it helps us see this less as a simple compliance challenge and more as a means to add genuine value to the company.

In FY04, we restructured our programs for environmental safety and health, posting and filling two positions focused on achieving excellence in the field. Also in FY04, a third-party auditor (Aon Risk Services), noted a 20 percent improvement in Nike's safety and health audit scores over FY03.

We are building an infrastructure for driving and improving performance, developing our capacity to collect data and report on any progress we're making. In FY05, Nike globally began using a common recordkeeping protocol we built the previous year.

Pressurized Cushioning

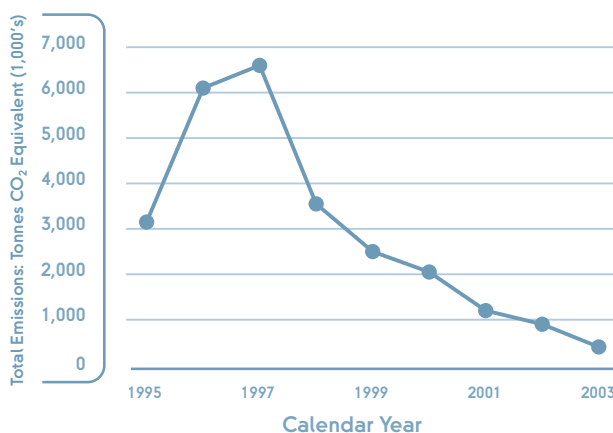
Nike first began incorporating pressurized cushioning into athletic shoes in 1978 because of the superior cushioning and impact shock protection they provide athletes. In 1992, we learned that although the gas used for pressurized cushioning, sulphur hexafluoride (SF₆), significantly improved the quality of our product, it was a greenhouse gas.

After years of research and tens of millions of dollars in capital and technology investments, we developed an encapsulation technology and a benign gas, nitrogen, that met our performance standards and did not contribute to global warming. Nike discontinued

the use of SF₆ in June 2003 and is currently pursuing a voluntary elimination of greenhouse gases in all its pressurized cushioning footwear products. Today, the majority of our footwear incorporating pressurized cushioning contains nitrogen.

However, for a period of time and for a limited number of high-performance models, technical challenges require us to use perfluoropropane (PFP, or C₃F₈) instead of nitrogen in order to meet the performance demands of pressurized cushioning platforms. PFP has nearly half of the climate impact of SF₆, allowing us to reduce greenhouse gas emissions while making the transition to nitrogen. Our global goal is to be able to offer nitrogen solutions across the whole of our product range by June 30, 2006.

Annual SF₆ and C₃F₈ Emissions



Notes: C₃F₈ is also known as PFP.

Assume all gas is emitted in the year it is filled into product.

Source: Calculation based on Nike purchase records.

Data relates to calendar year as required by the WWF Climate Savers agreement. Refer to Section CO₂ and Climate.

Water Quality and Conservation

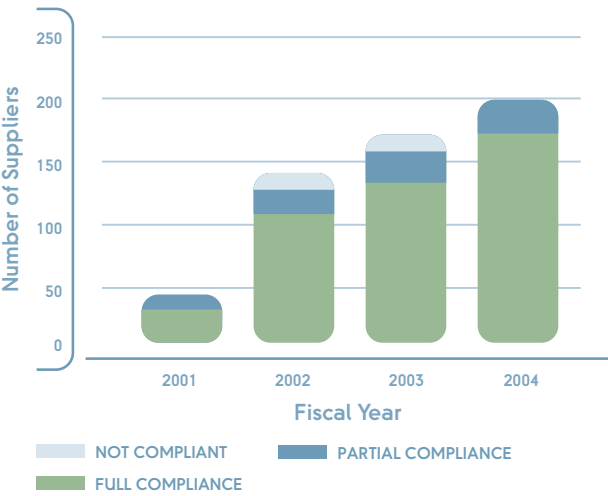
Protection of water resources is a pressing global priority. One-third of the world's population lives in countries suffering from moderate-to-high water stress. Nike is addressing water-related effects because the use of water and the discharge of wastewater

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from textile production facilities are the largest environmental and community impacts in apparel and textile production. Nike’s water program focuses on wastewater generated at Tier 3 facilities that dye, finish, launder or produce the textile materials used by cut and sew facilities to make our products. We encourage the use of water-efficient production methods and work with suppliers to bring their wastewater into compliance with a set of global water quality guidelines developed through a Business for Social Responsibility (BSR) consortium. We direct our suppliers to meet these standards or their local or national laws, whichever are more stringent.

Chart A illustrates the increase in the number of suppliers participating in the program each year, as well as improved compliance with Nike Apparel’s Global Water Quality guidelines. Participation has grown to include 280 suppliers in FY04, compared to 40 suppliers when the guidelines were rolled out in FY01. Of these 280 suppliers, 197 submitted the self-reported data and lab test results of wastewater needed to determine their compliance with the program. A supplier is considered to be in compliance if they are within 20 percent of the limits for each parameter of BSR’s Discharge Limits, and comply with all local/country discharge regulations.

Chart A
Apparel Tier 3 Compliance to Nike Global Water Program*



*Or local/national water quality standard, whichever is more stringent.
Partial compliance: Does not meet all parameters for local wastewater discharge standards.
Full compliance: Meets all parameters for local wastewater discharge standards.
Source: Wastewater samples submitted to Nike-approved testing labs and reviewed by CH2M Hill.

In the area of water conservation, Nike is working with textile suppliers to minimize the use of precious water resources and promote better water management practices in process operations. In FY04, we surveyed the supply base to determine what conservation methods were being used. The next phase will include the development of best management practices (BMPs) for water minimization and management and the dissemination of the BMPs among textile suppliers in over 25 countries.

Chart B illustrates the self-reported results of a FY04 survey of 197 apparel suppliers regarding implementation of water conservation methods.

Chart B

Apparel Percentage of Suppliers Implementing Water Efficiency Programs



Source: Vendor response to Nike Annual Water Quality Survey.

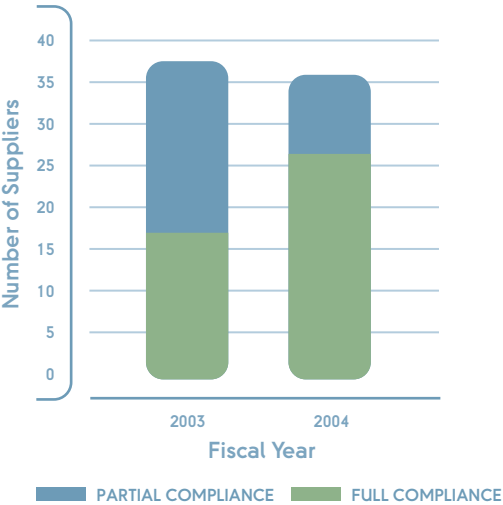
Footwear

The most significant impact from water use in our contracted footwear factories is on the use of water for domestic purposes. Nike is tracking this water use and directing our contract factories to meet local wastewater discharge standards. In some cases, Nike has required factories to install wastewater treatment facilities where local capabilities did not exist.

Chart C illustrates the self-reported results for footwear contract factories.

Chart C

Contract Footwear Factories Compliance with Local Wastewater Standards*



The long-term goal of Nike’s footwear division is to ensure that its supply chain meets water quality guidelines, focusing first on Nike contract manufacturers and on those materials that have a high probability of negatively affecting water quality.

The long-term goal of Nike’s apparel division is to ensure that its relevant Tier 2 and 3 suppliers meet the Global Water Quality guidelines or their local or national law, whichever is more stringent. In the next fiscal year, Apparel will be developing a strategy to further promote water conservation within its supply chain.

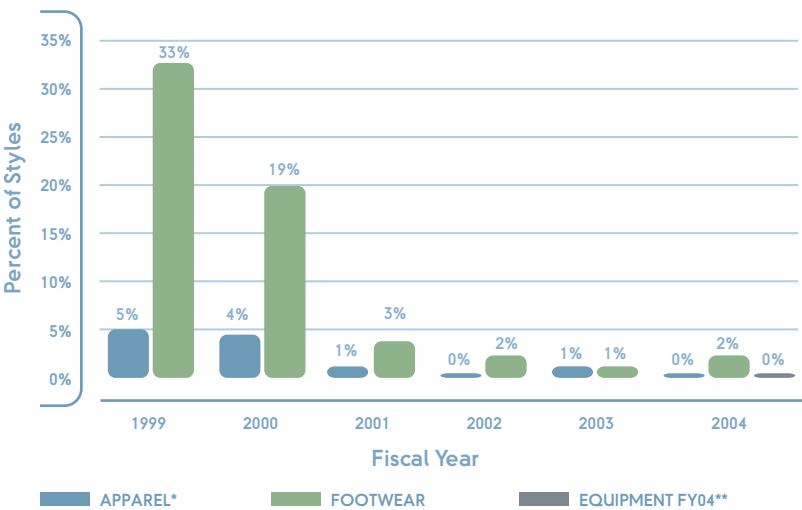
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Phasing out PVC from Nike Brand Products

Polyvinyl chloride (PVC), a material linked to a host of environmental concerns, is everywhere in our industry and in many others. While PVC is not widely banned by legislation, Nike voluntarily chose to eliminate the material from its products. Removing it from our product lines has required great cooperation in our supply chain and discipline from our design and production teams. We're not 100 percent PVC-free, but have made significant progress. For the few remaining product uses, performance and price have been the primary obstacles in the development of suitable PVC alternatives. Apparel still faces challenges with screen prints, heat transfers and

dimension weld embellishments. Nike and our ink suppliers and printers have spent five years working on ink and printing technologies that would meet our performance and aesthetic requirements. Today, we have technically feasible replacements for most of our basic inks, but the current price is substantially higher than traditional PVC-based ink. We are now working with ink suppliers and our supply base to determine how we can reduce this increase to a manageable level. In addition, with our current product data management system, we cannot track which ink systems are used by apparel factories. We will evaluate our business processes in FY06 and develop a strategy for creating a workable tracking method.

Apparel, Equipment and Footwear Percent of Styles Containing PVC



FY04 is the first year we began formally tracking PVC phase-out in equipment.
* Does not include screen print and heat transfer data for Apparel.
** Does not include Golf, Timing, Vision and Audio Equipment.
Source: Vendor self-reporting.

ELIMINATE WASTE AND TOXICS

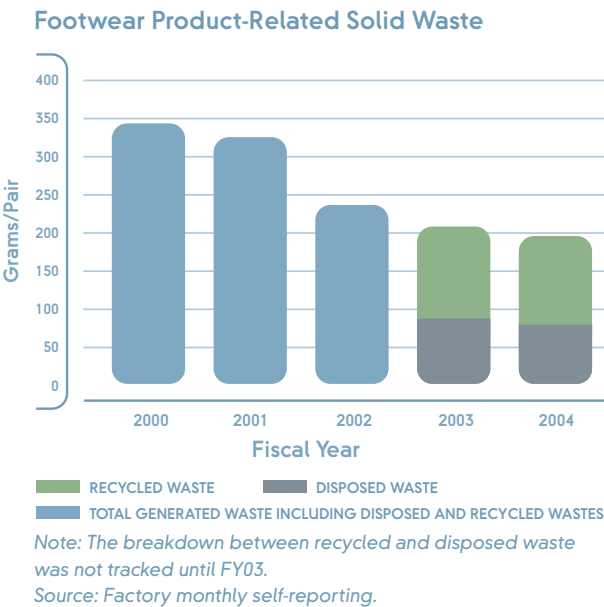
Solid Waste Elimination: Focus on Footwear

The challenges of solid waste management are numerous, especially within a contracted supply chain. In the mid 1990s, Nike Footwear began efforts to develop reliable systems for managing the waste generated from our products' manufacture.

Our first effort was to ban the use of on-site incinerators (typically used in Asia), which are inefficient and polluting; all incinerators have been removed from our contracted footwear factories. Working with factories, we have helped develop viable recycling infrastructures,

and have established waste management centers in several countries. For example, rubber scrap waste, previously managed as a fuel source in inefficient and polluting incinerators, is now re-incorporated into our outsoles or our Nike Grind licensing program (see *Recovered Product* section).

We have streamlined data collection by using environmental reporting software, which provides Nike with an integrated process for collecting, recording and monitoring factory solid waste management.



We are now in position to establish clearer goals for waste management for our contracted factories and their suppliers. Because we better understand the sources of waste generated from our designs, our internal teams can focus on the gradual elimination of waste. Footwear is currently developing a five-year stretch reduction goal that will be further defined in FY05 with our design, innovation and manufacturing teams.

Though we face different challenges with our apparel and equipment product solid waste, we will use our

footwear experience to move toward our strategic waste elimination goal across all of our products.

CO₂ and Climate¹

Because carbon dioxide (CO₂) emissions contribute to climate change, we are working to reduce these and other greenhouse gas emissions from our operations and those of our contractors. Changing and less predictable weather patterns potentially could affect consumer buying patterns, production locations, product shipping and even the cost of insurance coverage to facilities.

By the same token, if we're smart about our climate strategy, we also see that energy efficiency measures can help reduce our costs. In a world where fossil fuels become increasingly expensive, a transition to more green energy source could put us ahead of the predicted cost curve. Reaching future targets, once they are formalized, may enable us to see revenue generated from carbon trading and promote legal compliance with regulations emerging in different parts of the world.

Nike will continue to demonstrate its support for the objective of the Kyoto Treaty – reducing human-created emissions that contribute to climate change. This strategy was articulated in a 2001 voluntary agreement defining Nike's participation in the World Wildlife Fund's Climate Savers program. Through Climate Savers, Nike committed to reduce the combined CO₂ emissions from owned facilities and business travel by 13 percent by 2005 from a 1998 baseline. We also committed to create a baseline and define best practices in contracted product manufacturing and logistics services. The relative proportion of these contracted operations is shown in the following chart.

¹All data for CO₂ relates to calendar year rather than fiscal year; this is required by the Climate Savers agreement.

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We also voluntarily committed to a program and schedule to remove all greenhouse gases from products (see prior section, *Pressurized Cushioning*).

By the end of calendar year 2003, we were still working to meet the Climate Savers program goals. Since 1998, owned operations facilities have grown by 96,000 m² (8.5 percent); despite this growth, CO₂ emissions have returned to 1998 levels through energy conservation and green power purchases. Emissions from business travel are up 26 percent for the same period. Because we cannot affect fuel conservation on commercial air travel, we purchase offsets to reduce the impact of a portion of our business travel. Offsets are CO₂ reductions in projects outside of Nike (such as installing energy efficient lighting or fuel efficient boilers in public schools). Nike is committed to additional work to address the Climate Savers program goals through more action in all of these areas.

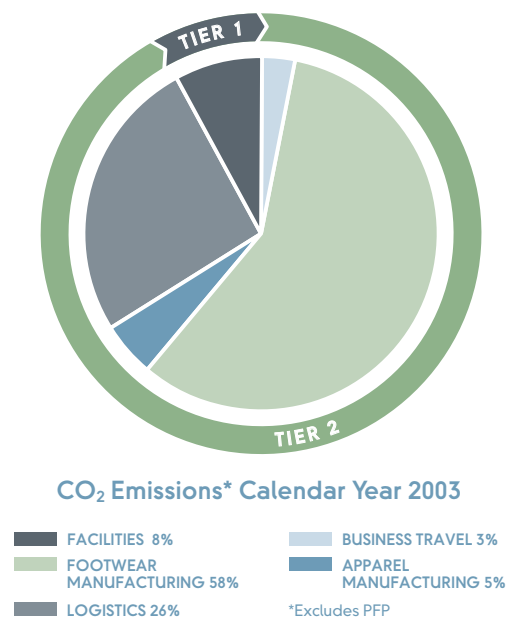
Contracted footwear manufacturing and product transportation are the areas of greatest impact and will be a growing focus of Nike's CO₂ reduction activities. Our global logistics staff has created a CO₂ model that calculates the emissions for every leg of all international shipments of Nike product, from the factory to the first distribution facility. As a member of Business for Social Responsibility's Clean Cargo Group, we are collaborating with a dozen companies to identify ways of reducing emissions from sea freight.

Nike has developed a system to identify and measure energy use from contract footwear factories. More than 50 percent of footwear production has been measured to date, and was used to provide the CO₂ emission data in the chart below. The goal is to develop a strategy around best practice, leading to a reduction in greenhouse gas (GHG) emissions from footwear manufacturing.

We plan to continue working to meet the Climate Savers goals that run through 2005. Nike's footwear division plans to develop a strategy and reduction targets by the end of CY05.

Chart A shows the relative proportion of the environmental footprint for CO₂ for Tier 1 (owned operations) and Tier 2 (contracted operations).

Chart A
CO₂ Emissions Footprint



Total: 1.2M Tonnes CO₂

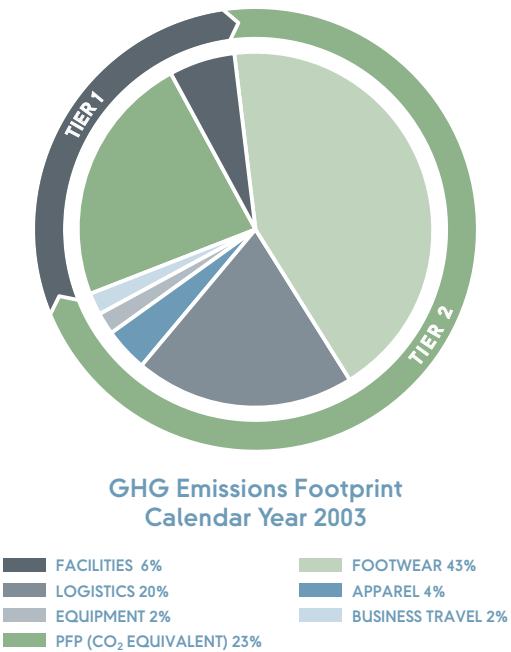
This chart mirrors the areas included in Nike's WWF Climate Savers targets. Emissions for equipment manufacturing are not represented because of their relatively small impact (two percent of the footprint, see earlier section, *Impacts and Issues*) and the diversity of manufacturing operations.

Source: Logistics – Emissions model developed by Nike and Univ. of Delaware. Facilities – Utility bills. Business Travel – Tickets and rental car report. Footwear – Facility self-reporting, scaled to 100% through engineering estimate. Apparel – 2002 Environmental Footprint Survey.

For more information please visit our website at <http://www.nikeresponsibility.com/climate>.

Chart B shows the relative proportion of total GHG emissions footprint for Tier 1 (owned operations) and Tier 2 (contracted operations) when PFP is included. Detail on the phase out of PFP is covered in an earlier section, *Pressurized Cushioning*. PFP is targeted for complete phase-out by June 2006.

Chart B
Total Greenhouse Gas Emissions



**GHG Emissions Footprint
Calendar Year 2003**

FACILITIES 6%	FOOTWEAR 43%
LOGISTICS 20%	APPAREL 4%
EQUIPMENT 2%	BUSINESS TRAVEL 2%
PFP (CO ₂ EQUIVALENT) 23%	

Total: 1.6M Tonnes CO₂ Equivalent

Note: PFP used in footwear is considered to be emitted from Nike-owned facility. Footwear footprint represents footwear factory energy use.

Source: Logistics – Emissions model developed by Nike and Univ. of Delaware. Facilities – Utility bills. Business Travel – Tickets and rental car report. Footwear – Facility self-reporting, scaled to 100% through engineering estimate. Apparel and Equipment – 2002 Environmental Footprint Survey. PFP – Calculation based on Nike purchase records.

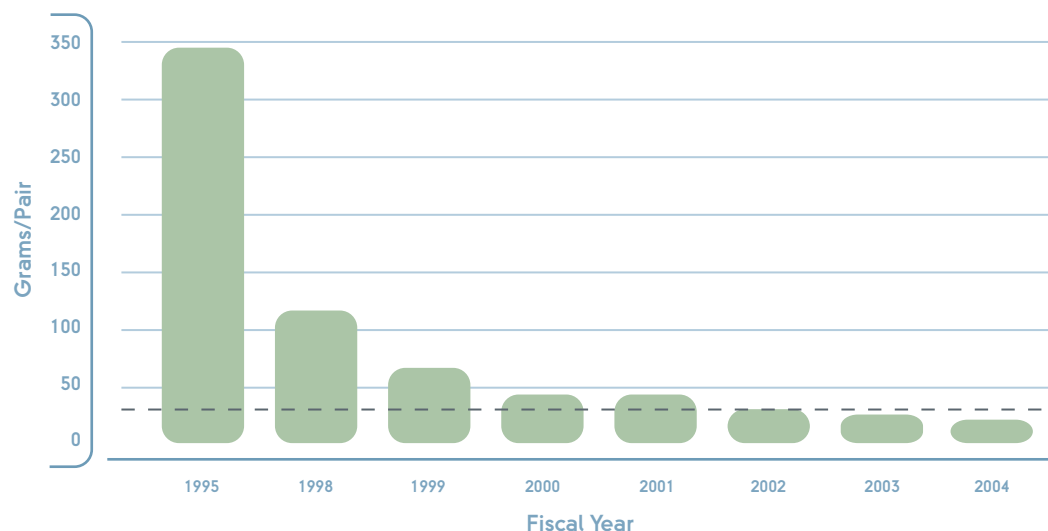
VOC Reduction

Volatile organic compounds (VOCs) are solvents used in manufacturing inputs such as adhesives, primers and cleaning fluid. These chemicals have the potential to be health hazards to factory workers and contribute to air pollution, particularly urban smog.

Since the early 1990s, we have focused on creating systems to collect solvent use data, monitor use and look for water- and detergent-based alternatives to solvent-based adhesives in footwear manufacturing. By working with suppliers, contract factories and some of our competitors, we have dramatically reduced the amount of VOCs used to make our footwear. This approach successfully reduced VOC use from an average of 340 grams per pair of shoes in 1995 to the current level of 16 grams. In some cases, sharing new technologies has promoted safer environmental practices as an industry standard. It should be noted that this goal applies to about 98 percent of Nike branded footwear. Two percent of our footwear is manufactured in South America for local markets and, owing to the relatively small volume, has not yet been included in the program.

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Footwear Volatile Organic Carbon Solvent Usage



• Baseline in 1995 estimated from chemical usage records.

• 1995 goal to reach 90% reduction obtained in 2002.

Source: Self-reported data from contract factories.

Our efforts to date have focused on our contract manufacturing operations; we are close to the limit of reduction with current technologies. Our initial VOC elimination goal was set in 1995 at 90 percent reduction. This was achieved in FY02. In the future, we will focus on design and innovation functions as an opportunity for further reductions.

SUSTAINABLE MATERIAL PLATFORMS

Organic Cotton

In fall 1998, we set out to successfully integrate organic cotton into our apparel products. Organic cotton is made without synthetic pesticides, fertilizers and defoliants. Because global supply didn't exist in sufficient quantity, we began working with farmers, spinners and textile mills to build capacity.

The entire value chain (farm through retail) must be engaged if organic cotton is to become mainstream. Nike worked with approximately 50 leading companies and organizations to form the Organic Exchange, an NGO aiming to increase organics' share of the global

cotton supply from the current level of about 0.05 percent to 10 percent. The Organic Exchange's three-year goal is to obtain brand commitments for organic cotton usage that total one percent of the average annual cotton production by the end of 2007.

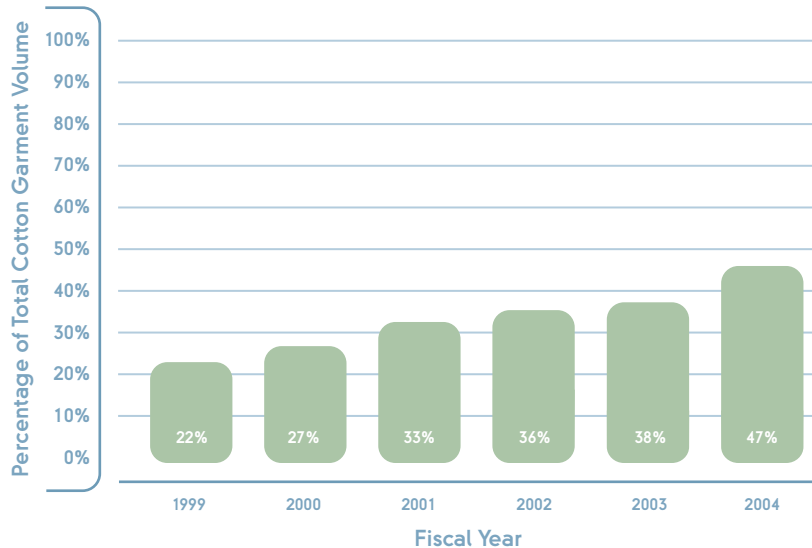
Our apparel business used approximately 52 million kilograms (115 million pounds) of cotton in FY04.

Twenty-two percent of our apparel cotton materials, and 47 percent of our cotton garments, contained a minimum of five percent organic cotton (more than double the number containing organic cotton five years ago).

In 2002, we introduced Nike Organics in our U.S. women's line, our first range of clothing made from 100 percent certified organic cotton. We followed it with similar offerings in U.S. men's, European women's and European kids' categories.

For more information please visit our website at <http://www.nikeorganics.com>.

Percentage of Global Cotton Garments Containing Organic Cotton



2010 Target 100%

Source: Nike Product Data Management System.

Nike's goal is for all cotton materials to contain a minimum of five percent organic cotton by 2010, equivalent to about 25 percent of the total current organic cotton world production. We will continue to seek opportunities to offer 100 percent organic cotton products as supply, logistics and price allow.

Environmentally Preferred Rubber

Rubber is an important performance material used in nearly all athletic footwear. Because our rubber formulations are usually mixed within our contracted manufacturing facilities, and millions of pounds of synthetic chemical compounds are batched, mixed and cured into our outsoles each year, we prioritized the development of an environmentally preferred rubber formulation. We started with our most commonly used rubber formulation and identified several synthetic compounds as chemicals of concern. These targeted compounds included accelerators, coupling agents, processing oils, fillers and other ingredients – all ubiquitous in rubber production.

Our goal was simple enough: Eliminate as many of these toxic chemicals as possible while still maintaining performance, price and aesthetics. The research performed to meet this goal fundamentally changes some of the long-held technologies within rubber production. The end result is that we have eliminated approximately 96 percent of the identified chemicals by weight in one of our highest-volume rubber formulations. In our introductory trial season (Spring 2004), approximately three percent of our models used the improved rubber formulation with no issues in commercialization or performance.

With this success, we project the use of the new rubber formulation to increase to approximately 60 percent of our models within the year. Our rubber advanced research team is now focused on product chemistry innovation in our remaining rubber formulations.

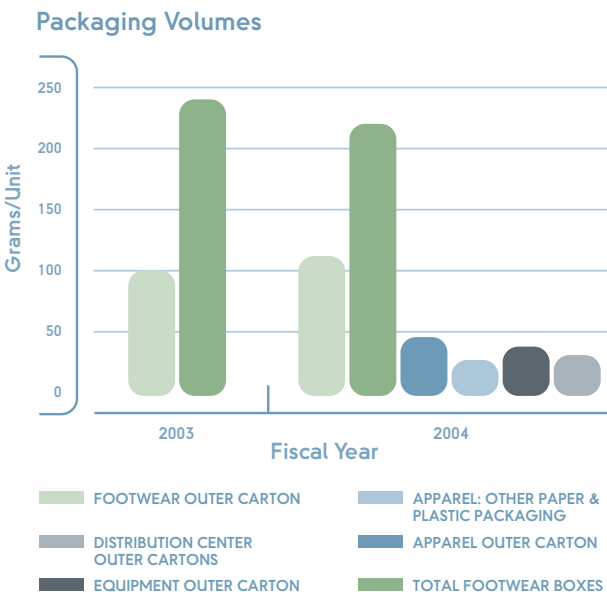
ENVIRONMENT

PACKAGING AND SHIPPING

Packaging, by its nature is destined to be waste.

Shoeboxes constitute the majority of Nike packaging. Great efforts have been made to minimize the amount of material used in the shoebox. Between 2003 and 2004 the final phase-in of a design change eliminated a total of 16 percent of the cardboard from an already efficient corporate shoebox. In addition, most of the shoeboxes are made from 100 percent recycled content and 80 percent post-consumer waste.

The table below shows the amount of consumer and transport packaging used by Nike.



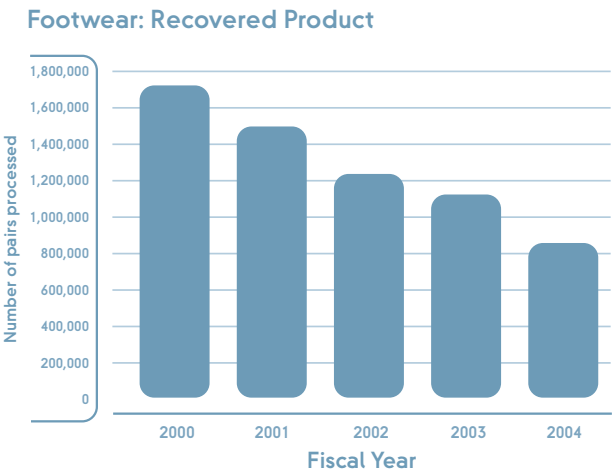
Note: FY04 was the first year data was collected for Equipment, Distribution Center and Apparel outer cartons and other packaging.
Source: Distribution Centers – Purchase orders for repack materials. Quantities ordered by factories from consolidated vendors.

We understand that there is a business opportunity to better manage packaging. We will continue to define and prioritize the potential packaging reduction projects – in business terms and in environmental

terms. Nike footwear is developing a five-year stretch reduction goal that will be further defined in FY05 with our design, innovation and manufacturing teams. Nike apparel is developing a strategy to address both packaging efficiency and reduction that will be further defined in FY06.

WASTE AS A BUSINESS OPPORTUNITY

Recovered Product



**Note: Pairs processed includes defective returns and post-consumer shoes. We have not collected the data in a segregated manner.*
Source: Reuse-A-Shoe Production Summary Report.

Nike is investing resources to significantly reduce the environmental impacts at the end of product life. Our Reuse-A-Shoe program collects worn-out shoes from consumers (any brand not containing metal) and defective shoes. The number of defective shoes has decreased over the past few years, and shoes donated by consumers have not yet made up the difference (see chart above)*. To increase the number of worn-out shoes collected, Nike partnered with the National Recycling Coalition (NRC) in the United States to expand shoe collection sites nationwide. Reuse-A-Shoe collection sites are now located within 15 miles of the homes of 32 percent of the U.S. population.

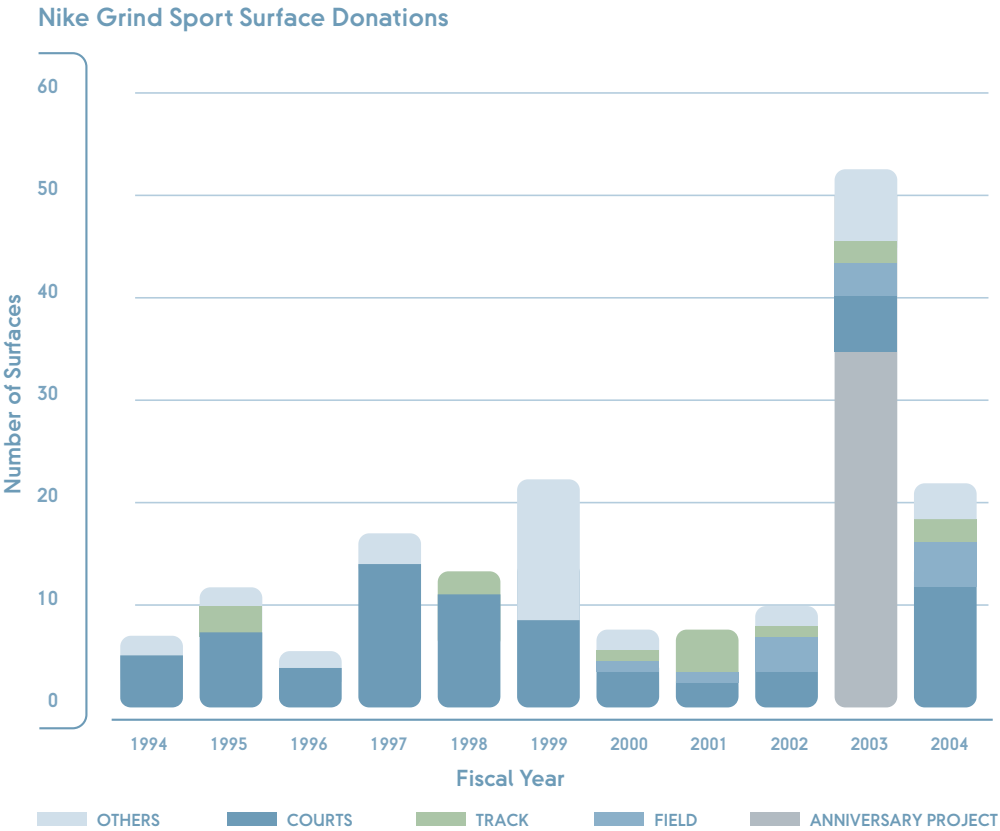
The shoes are separated and ground into three components at our Wilsonville, Oregon facility. The resulting material is called Nike Grind, of which there are three varieties – upper fabric, mid-sole foam and out-sole rubber.

Sports surface licensees use Nike Grind with other materials to make sports surfaces for soccer, football, baseball, basketball, tennis, running tracks and playgrounds. Nike Grind material from up to 100,000 shoes has been used in a running track, and over 15 million pairs have so far been processed for recycling. Even these numbers are a small fraction of Nike’s total production. Nike has used the experience of recycling materials from worn-out shoes to help find better uses for manufacturing scrap. Almost three million

kilograms of contract manufacturing footwear scrap has been used by licensees.

Nike uses the royalty monies from the licensees to help donate NikeGO sports surfaces to communities in need. Reuse-A-Shoe began in 1993, and since then, Nike has helped donate more than 160 sports surfaces. The program not only reduces environmental impacts of waste, but also benefits young people in communities lacking adequate sports facilities.

Reuse-A-Shoe is expanding globally. Australia’s program launched in 2003 and the United Kingdom’s began in calendar year 2004. We are actively investigating additional uses for Nike Grind and developing the means to recycle other Nike products.



Note: FY04 Anniversary Project included a donation of \$2 million to the city of Portland to refurbish over 192,000 square feet of sports surfaces that include Nike Grind material.

Source: Surface Donation Project database.

For more information please go to <http://www.nikereuseashoe.com>.

With the term “community investments,” we refer to Nike’s philanthropic contributions. We’ve made these kinds of contributions throughout the company’s existence. And increasingly, our employees are also making these kinds of contributions.

In the early years of our company, we had a clear focus for our community investments – though we neither deliberately chose the focus nor clearly articulated it. We supported athletes and sport. More specifically, we supported athletes we respected and sports we liked. We also kept things fairly close to home. It was a reasonable and fun approach for a small company.

For the better part of two decades, we were much broader in our support. We made contributions connected to more groups, and did so on a global basis. Our approach has continued to evolve. As this section will show, we’ve narrowed our focus, at least in terms of the kinds of issues we believe we can best address. And we’ve begun to be more rigorous in assessing the value of the contributions we can make.

IMPACTS AND ISSUES

Right to Sport and Physical Activity

As a leading player in the sports world, we’ve spent 30 years gaining insights into the role of sport and physical activity in people’s lives. We’ve commissioned research on the topic, and have relied on research funded by others. The findings reinforce our own sense of sport and physical activity and plays an essential role in the overall development of young people into healthy, confident adults. It is vital to healthy self-esteem. Yet across the globe, young people – particularly those excluded because of disability, poverty, race, religion or other social and economic factors – simply don’t have access to good, safe, enriching physical activity.

It is an issue with massive personal and cultural consequences. As the following research has demonstrated:

- Inactive children are less likely to graduate from school, more likely to use drugs and more likely to develop an eating disorder.
- Girls participating in sports are less likely to enter into violent relationships, suffer depression, become unwillingly pregnant or smoke. Yet girls drop out of sport six times more often than boys.
- Fifty percent of overweight 6-year-olds and 80 percent of overweight 12-year-olds will become obese adults.

What we've come to understand is that there are key ingredients – access points – for young people to improve their lives through physical activity.

- Access to facilities that are safe, affordable and accessible to all
- Access to inspiration such as coaches, mentors, athletes and others who provide alternatives to destructive behavior
- Access to opportunity with clear pathways for young people to pursue their passion for a sport in whichever way they want
- Access to continuity in sports and physical activity programs that are ongoing and consistently funded

Across the globe, the challenges unfold in different ways, often reflecting distinct economic and social factors. In Asia and Latin America, a core issue is the lack of access to the basic resources for sport and physical activity: facilities, equipment and coaches. Our focus is to work in partnership with others to provide facilities. In the United States and many other countries, the trend to youth inactivity has been rising for a variety of reasons: school funding cuts, lack of physical education programs, shortage of sports and play facilities, computers and the Internet, TV, and, occasionally, apathy.

Globalization

A second issue that our community work will increasingly aim to address is the challenge of globalization. We have chosen to focus on the specific challenges facing adolescent girls. The overwhelming majority of workers in our supply chain are women, most of them relatively young, and they live in cultures that have not always been inclined to expand the rights of women. Because of our supply chain's geographic distribution, some programs not specifically designed with gender in mind, nonetheless offer disproportionate aid to women. Our intent is to supplement those efforts.

We believe that investing in human capital complements our efforts to improve our fundamental business practices. We have learned that the most effective way for us to affect human capital may be to address the issues of poverty alleviation and gender equality, specifically by investing in efforts that empower the world's most disadvantaged girls to improve their well-being and participate more fully in life.

STRATEGY

Focus

A lengthy assessment of our community investments showed they were dispersed globally and by issue area. We decided to become sharper in our focus, and began assessing where we were having the most impact, where our values were best reflected and where our employees were most engaged. In 2002, we established two priorities for our community investment programs worldwide. The following two priorities guided our work in FY04 and will guide our work into the future.

First, we work to increase the participation of young people in physical activity, with a focus on the lifelong benefits it brings. We call this program NikeGO. We seek out opportunities to leverage all significant Nike resources, including athletes, products, cash grants, the power of our brand and employee passion in giving young people the opportunity to get active.

Second, we invest in innovative solutions that address the challenges of globalization, with a particular emphasis on women and girls. This acknowledges that Nike is often at or near the center of debates over globalization, that women are key to progress in the fight against poverty and inequity, and that women hold a majority of jobs in our supply chain. In FY04, this work was done through the Nike Foundation and the corporation. Going forward, it will be done through the Nike Foundation alone, the mission of which is to

COMMUNITY

contribute to poverty alleviation through improving the overall well-being of the world's most disadvantaged adolescent girls in the developing world.

Give Effectively

We think we can best contribute to communities in at least three ways: by promoting employee volunteerism and by giving cash and product. A fourth way involves giving our corporate expertise – insights into sport, marketing prowess, business modeling, etc. Sometimes, this can help our nonprofit partners better perform or deliver grassroots programs more effectively.

Volunteerism and Matching Employee Donations

Approaches to employee volunteerism and donations vary by global region, primarily for legal and taxation reasons, as well as the scale of the organizations involved. While there are established frameworks for corporations to match employee charitable donations in the United States, this is not the case in other countries. We are nonetheless committed to actively encouraging employees to be involved in the world around them. Globally, Nike managers are encouraged and actively support employee volunteerism.

If a U.S.-based employee contributes to a qualified nonprofit organization, we match their contribution, dollar-for-dollar, up to \$5,000 per employee per year. When a U.S.-based employee volunteers for a qualified nonprofit organization, we donate \$10 for every qualifying hour of volunteer work. In FY04, U.S. employees contributed 71,000 volunteer hours and gave more than \$2.5 million to hundreds of charitable organizations.

In Europe, employee activism is encouraged through our Sport4ACause Fund. When employees engage in charitable sporting events, Nike matches the funds they raise. In the UK, our EXTRA TIME program,

(started in FY05) gives employees six days per year for volunteer activities.

There are interesting implications in following the lead of employees. It can lead us to fund organizations we might not otherwise support. If such a contribution (directed by an employee) is taken out of context, it could drag Nike into controversy. We accept this as a possibility, and trust that, on the whole, encouraging our employees to be active will lead to positive ends for communities and for Nike.

EXAMPLES OF OUR WORK

Sport and Physical Activity

In Shanghai, most open-air basketball courts are located on school campuses where courts are locked up after school and on weekends, and at the times when young people most want to play. Since 1997, we've worked with Shanghai city and education officials to provide access to courts at five additional schools each year – with a total of more than two dozen playgrounds open as a direct result of Nike spending. This step inspired others. And hundreds of additional playgrounds are also open as a result of changed attitudes.

In Europe, middle-income families tend to have access to facilities and coaches while the poor and the excluded frequently do not. We focus on these excluded communities with programs that seek to directly serve refugees, migrants, the disabled or young people demonstrating behavioral problems. Much of our work is also focused on efforts that specifically aid girls from those communities.

The NikeGO Afterschool program, developed in collaboration with SPARK (Sports, Play and Active Recreation for Kids) focuses on those hours in the day when many young people find trouble. Designed

for YMCAs, local parks and recreation centers, Boys & Girls Clubs and others, Nike and SPARK provide training, custom curriculum and equipment to after-school program staff. It's fun, provides sport and physical activity options in which young people are constantly moving and helps each person feel successful. Staff and coach training is critical to ensuring that participants stay active once they are engaged. In addition, NikeGO has partnered with Stanford University's Positive Coaching Alliance to train coaches and parents to deliver enhanced coaching experiences to young people.

Globalization, Women and Girls

Nike contributions have helped develop solutions to the challenges globalization brings to women and girls.

- From 1997 to 2004 in Southeast Asia, our support of micro-loan programs has played a small but direct role in diversifying the ranks of small business owners. With the help of NGO partners, our funds become small loans, typically a hundred dollars or less, to individuals starting or growing a business. The vast majority of loan recipients have been women, who gain the flexibility to work at home. Since 1997, we have invested more than \$2 million in support of micro-loans. With our support, nearly 15,000 largely female borrowers in Vietnam, China, Indonesia and Thailand have received loans. In many cases, the loan recipients also benefit from training and education provided by the NGO. For more information on these partners, please visit our website at <http://www.nikeresponsibility.com/community>.
- In Thailand, we work with a key supplier and an NGO to bring production jobs to rural areas. Most Thai production jobs are based in major cities, and young people must leave home to find work. We recently renewed partnerships to expand the Nike Village Development Project in Nakhon Ratchasima province. Through the creation of a small stitching

center in the community, Nike Village offers about 500 villagers, primarily women, the opportunity to return to their homes and families from jobs once held in Bangkok. In addition to micro-loans, components will include a mobile AIDS unit, environmental reforestation to promote forest conservation, school lunch programs, mini-farms that produce high-quality products using limited natural resources available, sports activities and facilities, and development and training programs for women. By shifting away from the massive factories typical of our industry, we help families stay whole.

Moving forward, the focus on globalization will be absorbed into the Nike Foundation.

BUSINESS INTEGRATION

Community investment programs are part of a delicate balancing act in every corporation. They can be integrated into the business in order to leverage business expertise for community programs. But when a community program is driven only by business objectives, it can sometimes skew the outcomes of a program. We're clear: Community programs should measure success in terms of the impact they have on the ground and the difference we make. Marketing objectives flow from the extent to which we are successful on the ground. They're an outcome, not a driver.

At present, we have a community team based within both the United States and the EMEA regions, with a global community function carrying out both local (Oregon-based) activities and some global activity in regions where we don't have a strong community team in place. Going forward, better integration into the regional business teams in the Asia-Pacific and Americas regions is needed. More regional ownership of these programs is essential.

COMMUNITY

MULTI-STAKEHOLDER INITIATIVES

The majority of our community affairs programs are carried out in partnership with NGO's, and often with governments. That makes community affairs a hotbed of learning for us around multi-stakeholder partnerships. In working with the United Nations High Commission for Refugees (UNHCR), the U.S. Surgeon General and Mercy Corps, we've learned that each partnership is unique and requires unique attention. We've learned that if we're to take best practices to scale, we must occasionally work with our partners to engage in public policy advocacy.

In several global regions, we have advocated public policy changes, recognizing that solutions will be complex, long-term and will require support from all sectors of society. In the United States, Shaping America's Youth (SAY) was co-founded by the Surgeon General, Nike, the American Academy of Pediatrics and others; it is a national initiative devoted to promoting childhood sport and physical activity and healthy lifestyles. In Europe, we helped start the GO Network, which brings practitioners together to create a common voice and to share best practices. Examples of some of our external partnerships are as follows:

King Baudouin Foundation

The mission of the King Baudouin Foundation is to help improve living conditions for the population of Belgium and Europe. Nike funding provides support for sports programs that demonstrate the value of sport as a tool for social cohesion and integration.

Mercy Corps

Mercy Corps is an international organization that provides emergency relief, supports sustainable communities and promotes civil society initiatives in 76 countries. Since 1979, they have provided \$710 million in assistance, attempting to alleviate suffering, poverty and oppression by helping people build secure, productive and just communities. In FY04, Mercy Corps received over \$3.18 million in support from Nike.

United Nations High Commission for Refugees (UNHCR)

Nike's EMEA offices partnered with the UNHCR to pilot a sports program for young girls in refugee camps in Kenya. The goal is to use sports to promote girls' integration in education; sports can begin a process of opening doors and building respect.

National Head Start Association

Created in 1965, Head Start is the most successful, longest-running, national school readiness program in the United States. It provides comprehensive education, health, nutrition and parent involvement services to low-income children and their families. More than 21 million preschool-age children have benefited from Head Start. Nike is one of several organizations that has been honored for its commitment to Head Start and support of early childhood education. For the past six years, Nike has worked with Head Start on a state-of-the-art educational outreach program, making Nike one of the largest corporate supporters of the national school readiness program. Nike funded \$800,000 in FY04 as an investment in all communities.

Youth Sport Trust

Youth Sport Trust is a nonprofit organization that develops and implements quality physical education and sports programs for all children ages 18 months to 18 years. They believe that all children have the right to experience and enjoy physical education and sports. In this spirit, Nike donated \$410,000 in cash and \$360,000 in product throughout FY04.

Opportunity International

Through Opportunity International in Indonesia, Nike's micro-enterprise efforts have benefited approximately 11,500 borrowers. According to Opportunity International, Nike's partner to help deliver micro-loans to individuals near Jakarta, Indonesia, since 1998, Nike is one of the largest corporate funders of micro-enterprise development programs in the world.

Population and Community Development Association (PDA)

In Thailand, we support work by the PDA designed to improve lives in rural areas. While more businesses are relying on larger contract factories in already-crowded cities, PDA is helping build networks of smaller factories in rural areas, which means families stay united, and young people can stay at home and find meaningful work.

Positive Coaching Alliance

NikeGO creates and supports programs for inactive kids and the people who can influence their behavior: parents, teachers and coaches. The Positive Coaching Alliance is a Stanford University program that trains coaches and parents to deliver enhanced coaching experiences to kids in sports, so they have fun and are more likely to stay in the sport.

The Nike Foundation

The Nike Foundation’s mission is to contribute to poverty alleviation through improving the overall well-being of the world’s most disadvantaged adolescent girls in the developing world.

The Nike Foundation partners with private foundations, governments, NGOs and other organizations to ensure policies, strategies and investments reflect the critical needs of adolescent girls living in the developing world including education, health, economic opportunity, rights, voice and security. Among the Foundations’s partners are the International Center for Research on Women, the Population Council, Mercy Corps, the World Bank and the United Nations Foundation.

The work is focused in countries where the need is greatest. In some cases, this coincides with areas where we have a contract manufacturing presence. In

Bangladesh, for example, the Nike Foundation partners with BRAC, one of the world’s largest and most respected NGOs; BRAC reaches 1,500 communities and provides approximately 45,000 girls with access to safe places and economic opportunity. Also in Bangladesh, we are partnering in a \$50-million, five-year World Bank ROSC (Reaching Out-of-School Children) project to reach the hardest-to-reach children, especially girls, in ultra poor communities. The objective is to reduce the number of out-of-school children by about half a million, through improved access, quality and efficiency in primary education. In Ethiopia, the Nike Foundation will be investing with partners around issues surrounding child marriage.

For more information on the Nike Foundation, please visit the website at <http://www.nikefoundation.org>.

PERFORMANCE

A Commitment to Community: Nike’s Three Percent Target

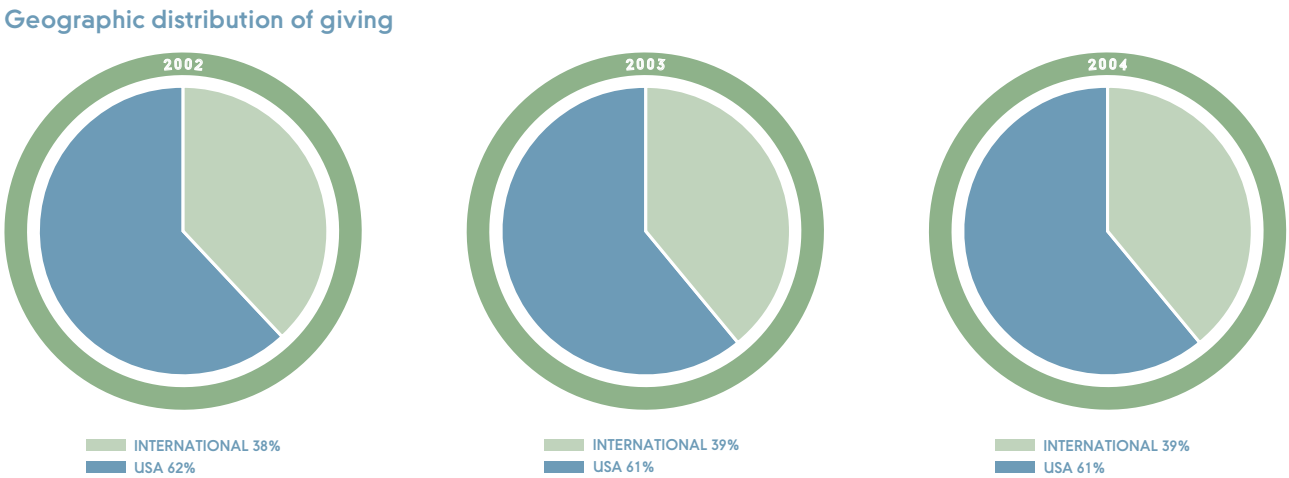
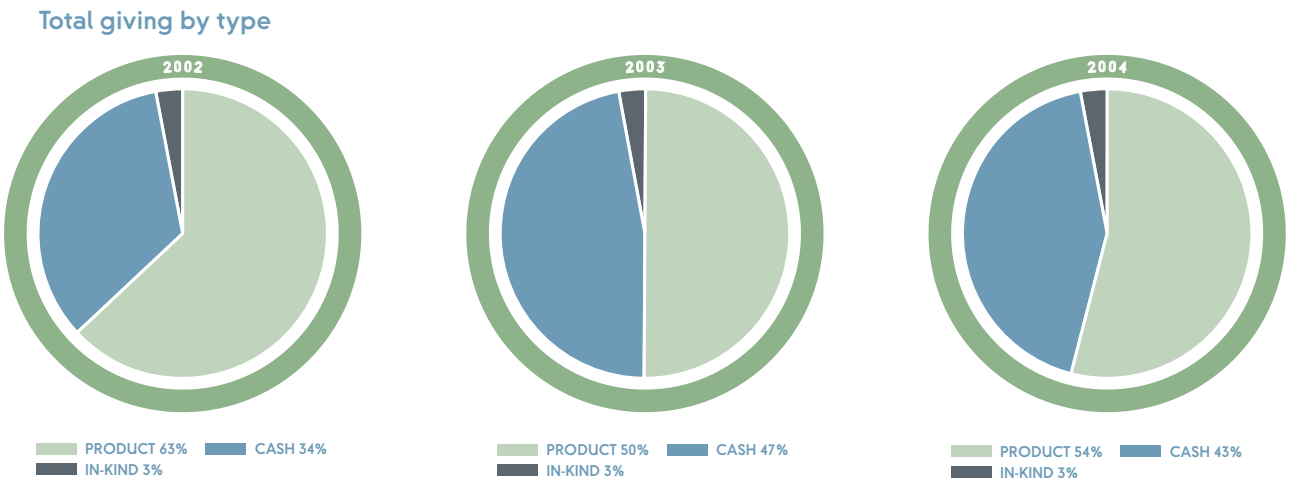
While community engagement has been a part of Nike’s culture since the beginning, in 1999 we formalized this commitment with a global target for contributions to nonprofit organizations and community partners. The target is three percent of the preceding fiscal year’s pre-tax profits. These gifts are a combination of cash, products and in-kind services.

Data

Total Donations (millions)	FY02	FY03	FY04
Cash	10.2	14.4	16.2
Product/In-kind	19.4	16.3	21.1
Total Donations	29.6	30.7	37.3
As % of prior year’s pretax profits	3.2%	3.0%	3.3%

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Employee Contributions and Company Match				
	Employee contributions	Employee hours match	Total company	Increase over previous year
FY02	\$1.8M	51,165	\$2.2M	11%
FY03	\$2.3M	67,212	\$3.0M	38%
FY04	\$2.5M	71,017	\$3.1M	6%



Fiscal Year

Assessing Impact

Beyond tracking measures of activity, we have been exploring various methods of assessing the impact of our community investments and their success in achieving stated objectives. In many cases, Nike relies on third-party experts to conduct these assessments.

In the United States, NikeGO has relied on experts from the Centers for Disease Control and Prevention to evaluate the impact of our programs. In Europe, Citizenship CSR Consultancy has conducted an extensive evaluation of our programs. We plan to continue to expand these types of assessments in the future.

THIRD PARTY EVALUATION OF NIKE COMMUNITY AFFAIRS PROGRAM IN EMEA

Citizenship CSR Consultancy was hired by Nike in 2003 to conduct a third-party assessment of the impact of its EMEA program.

Program Objectives

The stated aim of Nike's community program in EMEA is to support projects that use sports as a catalyst for social inclusion, especially among young people. This is an ambitious goal, since social inclusion depends on people developing life skills as well as job skills, and having positive attitudes, good behavior and work opportunities. It is only when we start to assess all these factors that we can judge the real impact on the lives of young people.

Methodology

Our aim was to go beyond simply reviewing the resources invested and to assess real social impact. We found this was best measured by the participants themselves saying how they felt better or different, and by third parties saying how they saw changes taking place in people they knew.

A snapshot of activities and impact

- Projects in seven countries with diverse social settings
- Ninety-five different community initiatives
- Contributions from 1,500 to 400,000 Euros per project
- Projects managed through foundations with community partners and via volunteering
- Fifteen thousand disadvantaged individuals touched through over 1,500 sports or sports-related sessions

Nike's projects included helping get young people into employment or full-time education in Belgium; touched over 2,200 disadvantaged young people in the Netherlands and significantly affected about 75 percent of them in terms of social integration; worked with kindergarten and disabled people in Germany; promoted large projects for primary school children and girls in sports in the UK; assisted people with disabilities in Spain; and led a range of sporting initiatives for disadvantaged young people in South Africa. At the time of the review, the program in France was still under construction.

Conclusions

The program responded well to Nike's objectives:

- Nike's sports and sports-related projects were clearly effective in reaching disadvantaged groups, and often gained sustained levels of participation even among disaffected youngsters.
- Project assessments showed many examples of real social impact, with demonstrable results in terms of life skills, socialization and self-esteem.

At the same time, the program had flaws:

- Many of these assessments could be greatly strengthened by clearer objective-setting and a focus on tracking outcomes.
- There was also a case for reviewing the rather wide diversity of project sizes, national focus topics and project management mechanisms.

Finally, Nike's work suggested some lessons for others:

- The program's results give real backing for the value of sports in reaching disadvantaged groups.
- This may have special merit among young people, for whom sports are cool and can bridge divides of culture, language, race and color.

Source: Nike's Community Investment Impact, 2002-2003, Citizenship CSR Consultancy, Stephen Serpell, Director, Citizenship CSR Consultancy, UK

For more information on Nike's work in this area, you can download our FY04 community development report at <http://www.nikeresponsibility.com/reports>.

ENGAGING WITH GOVERNMENTS

Nike has government affairs offices in Washington, D.C., Beaverton, Brussels, Beijing, Singapore and elsewhere because we recognize that government action, particularly on trade matters, can significantly influence the success of a global business. The 12-person staff leverages its size by working closely and collaboratively with other Nike departments.

Whatever access we have to political figures is based on a combination of factors some of which may be unique to Nike. These factors include the strength of our brand, the number of jobs we represent in a given region, and our ongoing efforts to build relationships on a bipartisan basis with a broad coalition of parliamentarians, senators, representatives, mayors, ministers, ambassadors and other national and local public officials.

In the United States, Nike's federal Political Action Committee (PAC) contributions amount to approximately \$50,000 annually (full disclosure on contributions by the PAC, or Nike executives is available at <http://www.fec.gov>). In 2003 and 2004, as in previous years, these funds were divided among members of both major political parties in both Houses of Congress who reflect our corporate values and business goals. We have been strong, public supporters of campaign finance reform in the United States; we never participated in soft money contributions when they were legal, and we are now

concerned about the influence of 527 committees, which fund issue advocacy campaigns but are often very clearly supportive of specific candidates. In part, our opposition to these contributions has always been a practical one, indicative of our approach to politics and government in general: The lack of transparency made it difficult to know how the money was spent and on whom. Outside the United States it is our policy not to make campaign contributions.

Approach to Political Outreach

Our approach to engagement with government and public policy makers is based on nonpartisanship, transparency and pragmatism. We tend not to use external consultants to represent us (we are the best advocates of our own business interests), and whenever possible lean towards participating in broad coalitions.

The policy landscape is constantly evolving, and our team across the globe may be engaged on issues related to international trade and customs, environment, tax, corporate responsibility, physical fitness, e-commerce and intellectual property protection. When deciding on issues, we try to consult a wide range of stakeholders, both internal and external. We focus on issues that are directly related to our business. We try to marshal our resources, taking positions strategically so we have impact once we speak out.

PUBLIC POLICY

Two environmental issues from 2003-2004 helped provide insight into how we make these choices. One involved working with members of Congress and other outdoor apparel companies to urge the U.S. administration not to abandon the rule prohibiting roads from being built in currently protected forests. The other involved legislation to prohibit oil drilling in the Arctic National Wildlife Refuge (ANWR), in order to protect wildlife. The two measures were met with similar arguments: One side said the issue was about protecting pristine wilderness lands, and the other said it was about protecting jobs and wisely using scarce natural resources.

Because the Roadless Rule could have an impact on the quality of wilderness areas in the lower 48 states, it is conceivable that it could enable more ACG (Nike's All Conditions Gear) customers to use our gear in those places. Many areas affected by the rule would actually be in our own backyard in Oregon. We also believe that supporting the Roadless Rule would enhance our relationships with outdoor retailers in the American West – a group that was important to our growing ACG business and with whom we wanted to develop closer relationships. We ultimately supported the Roadless Rule, joining in with a coalition of western outdoor retailers.

We did not take a position on the ANWR measure, as we determined that it was not related to our business. It was highly unlikely that our products would be used there, and there was no sense of an appropriate coalition for Nike to join.

Stands on Key Issues

Among our key CR positions in FY03 and FY04 are the following:

Permanent Partner benefits. In the United States, we actively promoted legislation to end discrimination on the basis of sexual orientation. We also supported a measure to end the taxation of health benefits that some employers, including Nike, provide to the partners of employees who are involved in same-sex relationships (these benefits are not taxed when granted to married couples). These issues directly affect our employee base, and are integral to Nike's commitment to improved workplace diversity.

Trade support to less developed nations. With the expiration of the Multi-Fiber Arrangement (MFA) on January 1, 2005, we will actively support legislation and regulation in the European Union, the United States and elsewhere that promote preferential or duty-free market access for apparel exports from developing countries that are expected to be hardest-hit such as Bangladesh, Cambodia, Vietnam and others. We believe such legislation and regulation will help preserve critical industries and jobs in these low-income countries.

Youth activity and sports participation. We are currently working in several regions with government, industry, academic experts and other stakeholders to develop and implement policies that encourage sports participation as a tool to tackle issues such as social integration and physical inactivity.

China and world trade. We continue to support China's membership in world trading bodies and regimes, stressing that full U.S. engagement with China and Chinese participation in global forums are the best means of achieving positive reforms within China.

Vietnam and world trade. We support continued trade status with Vietnam and will work to support granting Vietnam membership in the World Trade Organization (WTO), bringing them into the same set of rules as other nations.

Title IX. In the United States, through advertising and public policy advocacy, Nike has been a strong supporter of Title IX of the 1972 Education Act Amendments, which changed the face of collegiate academics and athletics. Popularly called Title IX, this law opened the door for women to pursue professional career paths and become full-fledged college athletes after decades of roadblocks that included gender bias and discrimination, arcane quotas and limited or non-existent collegiate athletic opportunities.

Membership in Business Associations

In addition to our own political outreach, we belong to multiple associations that play active roles in policy making. While we do not always agree with the positions taken by these organizations, we are members nonetheless because the organizations often provide important business benefits and opportunities for dialogue. Some of these organizations include the following:

- American Chamber of Commerce, European Union
- Beaverton Chamber of Commerce
- British Sports and Allied Industries Federation
- Business for Social Responsibility
- Council on Foreign Relations Corporate Program
- European American Industry Council
- European Policy Centre
- Federation of European Sporting Goods Industry
- Footwear Distributors and Retailers of America
- Geneva Business Round Table
- National Industrial Transportation League
- Oregon Business Association
- Oregon Business Council
- Portland Business Alliance
- Retail Industry Leaders Association
- Sporting Goods Manufacturers Association
- U.S. Chamber of Commerce
- U.S. Council for International Business
- U.S.-ASEAN Business Council
- U.S.-Vietnam Trade Council
- Waterfront Coalition (Washington, DC)
- World Federation of Sporting Goods Industries

CHALLENGES AND OPPORTUNITIES

09

Corporate responsibility can be a radar for the future, preparing us ahead of time for legislation, consumer expectations and challenge. At the same time, it helps us uncover new ways of doing business – ways that connect us to new and different consumers, reduce our costs, fuel innovation and creativity within the company, and generate intangible and tangible assets.

Identifying challenges is the key to unlocking the potential of corporate responsibility. The nature of challenges is that we don't quite know what will happen. This gives us the opportunity to envision new possibilities. With creativity and help, these business challenges can be turned into business opportunities.

Engaging with stakeholders has helped us identify a large set of challenges and dilemmas. We outline some of them here, with a focus on those that clearly represent both challenge and opportunity. We'll continue to seek help in wrestling with them.

China

China presents Nike with a myriad of challenges. We see ways to bring opportunity to workers there, but we also know that local laws and customs often make it difficult for us to accurately gauge conditions in factories. Rapid growth is having a significant impact on the country's environment, yet it may take economic growth to fund the country's environmental initiatives.

The tension in these challenges is heightened by the scale. We produce more goods in China than in any other country. In FY04, 36 percent of Nike footwear was manufactured in China in more than 17 contract factories. An additional 96 contract factories make apparel and equipment products for Nike. Our manufacturing needs result in the employment of more than

180,000 workers. Our sales presence in China is growing as well. Since 2003, sales of Nike product in China have grown at an annual rate of more than 50 percent.

Upholding our Code of Conduct with respect to the issue of freedom of association is an obvious challenge: Chinese law prohibits independent labor organizing. One view suggests companies should not bring business to China until freedom of association is granted to its workers. We believe that a policy of direct engagement and openness is the best path to reform in China.

We have the beginnings of an approach based on engagement and facilitating opportunities for parallel means of independent representation for workers in our contract factories. This reflects a commitment to

collaboration with local partners. Chinese stakeholders, including the government, are increasingly aware of social compliance issues and their impact on business relationships, and they are beginning to wrestle with these notions. Knowledge that supports worker rights is slowly being developed.

Beyond the issue of freedom of association, there are other obstacles to protecting worker rights in China.

- A pervasive lack of clarity over what constitutes law complicates monitoring efforts. Among the factors contributing to this are inconsistencies between national and local laws.
- Falsification of information by factories often related to wages and hours of work is common. This extends to the practice of coaching of workers by factory managers trying to deceive compliance auditors.
- The massive, temporary migration of workers driven from the rural areas into China's largest cities in search of employment has several effects, including putting workers in a vulnerable position because their jobs and access to social services depend on their employers applying for permits on their behalf. The Department of Labor of Guangdong Province, the premier export manufacturing region in China, estimates that there are over 26 million migrant workers in the region.

We have seen labor successes in China. For example, one Nike contract supplier has made important progress in aiding workers. They built affordable housing and made it possible for some workers to buy homes and gain local permanent resident status, with the benefits of schooling and medical care that come with local citizenship. They reduced the number of work hours while still increasing productivity, and installed a grievance system that allows workers to bring complaints to management. The company provides night-time access to high school and college educations.

China's explosive growth into an industrialized economy presents environmental challenges of a staggering scale. A World Bank study says 16 of the 20 most polluted cities in the world are in China, and millions of its people drink contaminated water. The consequences of environmental issues in China directly affect our suppliers: Electricity shortages are forcing many contract factories to build their own generators; and in some places, the burden of treating waste has shifted to the private sector as opposed to something managed by the government and paid through taxes.

Importantly, environmental issues are gaining increased attention from the government and from an emerging local NGO sector. Our challenge, and our opportunity, is to understand how we can reduce environmental impacts in our Chinese supply chain and, in doing so, promote sustainable approaches to business. Because the government of China is increasingly interested in addressing this issue, the opportunities for innovation in this context are growing.

Our most important steps in China may involve building partnerships. The complexity, severity and depth of the issues demand multiple voices and perspectives; strong partnerships may give them greater volume and visibility. The NGO tradition is largely absent and will take time to evolve, as will the practice of transparency. Our intent is to engage more often with local NGOs.

Multi-Fiber Arrangement

In February 2004, Nike hosted its first global stakeholder forum to receive feedback on emerging corporate responsibility challenges. One of the issues discussed at the forum was the potential impact of the upcoming phase-out of quota in the textile and apparel industries under the World Trade Organization's Multi-Fiber Arrangement (MFA).

CHALLENGES AND OPPORTUNITIES

The international Multi-Fiber Arrangement, also known as the Agreement on Textiles and Clothing, has regulated the flow of textiles to the United States and Europe for more than a decade. Its quota system gave many developing countries protection from global competition and, therefore, indirect support for their domestic textile industries. Because the MFA was phased out at the end of calendar year 2004, many textile producers in these developing countries must now compete in a quota-free environment.

In the long term, we believe the MFA phase-out is positive. For too long, production managers in our industry have spent time “chasing quota,” or placing and managing orders with new factories because other factories or other countries have already hit their quotas. This has contributed to the prevalence of short-term relationships between buyers and manufacturers across the industry. Short-term relationships are not always compatible with best practices on CR.

In the short and medium term, MFA phase-out may have negative consequences for some key textile and garment-producing countries, many of which have factories producing for Nike. The countries that are most vulnerable have been highly dependent on the textile and apparel sector for foreign currency generation, employment or tax revenues from foreign investments. Many of these countries have not built competitive textiles industries that are able to compete in a quota-free environment, and they lack the funds to invest in other industries or infrastructures that might enhance their competitiveness. Consequently, their workers may sink deeper into poverty. Other countries will gain textile jobs because they are better positioned to compete without quotas; the presumption by many is that China and India will be big winners.

While we are working to gain a better understanding of what, if any, shifts are likely to occur within our source base, our current strategy is not to make significant changes. We believe other trade barriers may be instituted to affect export flows. Our overall strategy is based on moving toward a more efficient sourcing base by expanding relationships with key manufacturers, some of which happen to be located in the countries identified as most vulnerable under the changed trade regime.

Nonetheless, the constellation of manufacturing is likely to change around us, regardless of what actions we take within our own supply chain. This is an issue that is beyond the scope of one company to address. Industry consolidation seems inevitable, although the time frame is unknown. To help us better understand the trends and impacts of quota elimination and, more importantly, to identify strategies to mitigate the impacts, we are participating in the MFA Forum convened by AccountAbility, a UK-based nonprofit organization. This group emerged from discussions held by a group of individuals at our 2004 stakeholder forum. We are also participating in discussions in several regions to explore mechanisms to protect workers who may lose their jobs as a result of the changing quota regime, or to enhance the competitiveness of vulnerable industries. We don't yet know what the exact impacts will be, but we do know that we can have far greater influence on them if we engage on this issue and do so collaboratively.

For more information about the MFA Forum, see the *Workers in Contract Factories* section.

Bringing CR to Our Subsidiaries

Readers will note that nearly all of this report applies only to products made under the Nike and Jordan brands. We have a growing portfolio of brands as

outlined in the *Company Profile* section of this report. Today, these other brands make up 11 percent of our sales revenue – a percentage that is likely to grow in years to come.

We have not yet developed a corporate responsibility program for our growing portfolio of brands that would cover the full set of areas addressed within the Nike brand, including supply chain compliance, sustainable product, community investment, human resource management and diversity. We have taken initial steps to supplement work that existed prior to our acquisition of these companies, including the preliminary integration of Cole Haan, Bauer Nike Hockey and Converse into our supply chain compliance activities. Our challenge is to define CR standards for acquisitions, clear strategies for bringing our CR values to acquired brands, and reasonable timelines for doing so. The opportunity is to take the learning from our work with the Nike brand, and consider which approach is likely to be the most appropriate and have the greatest impact within the different brands that make up Nike, Inc.

We will be working in FY05 to develop our plans and toward a timetable for addressing CR in all of our brands.

Stakeholder Engagement

Over the past 10 years we have focused most of our engagement of civil society around corporate responsibility issues. We've learned a great deal from this interaction. NGOs and others have opened our eyes to new issues and viewpoints, and have enabled us to draw on their experience and expertise. More recently, we have begun to develop more structured engagement processes, starting with our stakeholder forum and the report review committee for this report. We have much more work to do in this area to

achieve greater levels of consultation, including with our keenest critics – many of whom we engage often around specific incidents, usually around discoveries of non-compliance by our contract factories. Going forward, we recognize that it will be critical to build systems and processes that allow external stakeholder voices to be heard more deeply within the business. Closing the feedback loop back to stakeholders is another important step in this process.

Transparency

Transparency isn't really a dilemma for us. We're very clear about it: We believe in it, know its value and understand its importance. But it is a risk. And an opportunity.

The risk is that what we say can be taken out of context. In the complex world of corporate responsibility, that can be difficult, particularly without uniform reporting standards to ensure a fair and accurate interpretation of the data presented. The first hard lesson of transparency is that bad news trumps good news. The best response is probably not to focus on good news or bad news, but on more and better transparency.

Transparency is an opportunity, if driven by a desire, to inform stakeholders and enable them to make informed judgments about us based on the facts. It can only be a driver of broad societal change if it is adopted by more than a handful of companies.

This is especially true for transparency around contract factories. We believe that disclosure of supply chains is a key to unlocking greater collaboration among brands and to creating the incentives necessary for factories to turn their CR performance into a point of differentiation.

This report reflects our genuine desire to inform. We hope it has succeeded. Please let us know.

GRI INDEX

GRI Indicator			Corresponding Global Compact Principle
Indicator	Description	Section/Notes	
1. Vision and Strategy			
1.1	Vision and Strategy	Part II - p. 9-12	8
1.2	CEO Statement	Part I - p. 3	
2. Profile			
2.1	Entity Name	Part II - p. 1	
2.2	Major products/services/brands	Part II - p. 1	
2.3	Organizational Structure	10K	
2.4	Divisional Descriptions	10K	
2.5	Global Operations	Part II - p. 2-4 (B)	
2.6	Legal Ownership Structure	10K	
2.7	Market Description	10K	
2.8	Organization Size	10K	
2.9	Stakeholder Relationships	Part II - p. 23, 30-33, 40, 48, 54-55, 60-62, 78-79, 85	
2.10	Contact Information	Part I - p. 10	
2.11	Reporting Period	Part I - p. 8	
2.12	Prior Reporting Period	Part I - p. 8	
2.13	Reporting Limitations	Part I - p. 8	
2.14	Business Changes Since Prior Report	10K	
2.15	Third-Party Reporting	(C) Not reported	
2.16	Restatements	10K	
2.17	Reasons for GRI Absence	(C) Not reported	
2.18	Criteria Used for Nonfinancial Measures	(C) Not reported	
2.19	Measurement Method Changes	10K	
2.20	Internal Assurance Process	Part I - p. 12	
2.21	Independent Assurance Process	Part I - p. 10	
2.22	Additional Information Source	Web: www.nikeresponsibility.com	
3. Governance Structure and Management Systems			
3.1	Board/Governance Structure	Web: www.nikebiz.com/boardofdirectors	
3.2	Independent Board Members	Part II - p. 5	
		Web: www.nikebiz.com/boardofdirectors	
3.3	Board Strategy Process	(A) Not reported	
3.4	Governance Processes	Part II - p. 6-7	
3.5	Executive Compensation	10K (B)	
3.6	Governance Responsibility	Part II - p. 7	

Key:

- (A) This information is not reported due to the absence of a formal system in place.
- (B) This information is partially reported, in accordance with systems currently in place as well as the current access to data.
- (C) This indicator is determined to be “not material” due to Nike’s lack of impact on this issue.
- (D) This information is not reported due to a lack of access to appropriate data.
- p Page Number
- 10K Indicates that this information is presented in the 2004 Form 10-K, filed with the U.S. Securities and Exchange Commission.

GRI Indicator	Indicator Description	Section/Notes	Corresponding Global Compact Principle
3.7	Internally Developed Principles and Policies	Part II - p. 5-6	
3.8	Shareholder Recommendation Process	Web: www.nikebiz.com (Investors section)	
3.9	Stakeholder Relationship Selection	Part II - p. 13	
3.10	Stakeholder Consultation Methods	Part II - p. 13 (B)	
3.11	Stakeholder Consultation Information	Part I - p. 11-12, Part II - p. 14 (B)	
3.12	Stakeholder Information Use	Part II - p. 13-14 (B)	
3.13	Precautionary Principle	(A) Not reported	7
3.14	Principles and Policies Endorsed	Part I - p. 8, Part II - p. 23	
3.15	Association/Organizational Memberships	Part II - p. 85	
3.16	Upstream/Downstream Impacts	Part II - p. 9-11	
3.17	Managing Indirect Impacts	Part II - p. 9-11	
3.18	Location Decisions	Part II - p. 1	
3.19	Performance Programs and Procedures	Part II - p. 33-46, 54, 62-73, 79-82 (B)	
3.20	Management Systems Certification Status	(C) Not reported	
4. GRI Content Index			
4.1	GRI Content Index	Part II - p. 90-94	
5. Economic Performance Indicators			
EC1	Net Sales	Part II - p. 2, 10K	
EC2	Geographic Market Breakdown	Part II - p. 2, 10K	
EC3	Cost of Goods, Materials and Services	10K	
EC4	Contracts	(C) Not reported	
EC5	Payroll and Benefits by Region	Part II - p. 53, (B)	
EC6	Capital Payments	10K	
EC7	Retained Earnings	10K	
EC8	Taxes Paid	Part II - p. 3, 10K	
EC9	Subsidies	(C) Not reported	
EC10	Donations	Part II - p. 79-80	
EC11	Supplier Breakdown	Part II - p. 4, (B)	
EC12	Non-core Business Infrastructure Development	(C) Not reported	
EC13	Indirect Economic Impacts	(C) Not reported	
Environmental Performance Indicators			
EN1	Materials Use	Part II - p. 70, (B)	8
EN2	Waste Percentage of Materials Use	Part II - p. 67, 72	8
EN3	Energy Use By Primary Source	(A) Not reported	8
EN4	Indirect Energy Use	Part II - p. 58	8
EN5	Water Use	Part II - p. 58, 63-65	8
EN6	Land Owned, Leased or Managed (in Biodiversity-rich habitats)	(C) Not reported	8
EN7	Major Impacts on Biodiversity	(C) Not reported	8
EN8	GHG Emissions	Part II - p. 63, 67-69	8
EN9	Ozone-depleting Substances	(C) Not reported	8
EN10	NOX, SOX and Other Emissions	(C) Not reported	8
EN11	Waste	Part II - p. 58, 66-67, (B)	8

GRI INDEX

GRI Indicator	Indicator Description	Section/Notes	Corresponding Global Compact Principle
EN12	Discharges to Water	(C) Not reported	8
EN13	Chemical, Oil and Fuel Spills	(C) Not reported	8
EN14	Environmental Impacts of Products and Services	Part II - p. 63, 70, 71, 72	8
EN15	Reclaimable Weight of Products	Part II - p. 72-73, (B)	8
EN16	Non-compliance Fines – Environmental Regulations	(C) Not reported	8
EN17	Renewable Energy/Efficiency Initiatives	Part II - p. 68	9
EN18	Energy Consumption Footprint	Part II - p. 58	
EN19	Other Indirect Energy Use	Part II - p. 68	
EN20	Water Sources Significantly Affected	(C) Not reported	
EN21	Annual Ground/Surface Water Withdrawals	(C) Not reported	
EN22	Recycling/Reuse of Water	Part II - p. 65, (B)	
EN23	Land Owned, Leased or Managed (Production/Extractive Use)	(C) Not reported	
EN24	Impermeable Surface	(C) Not reported	
EN25	Protected or Sensitive Areas	(C) Not reported	
EN26	Natural Habitat Changes	(C) Not reported	
EN27	Protecting/Restoring Native Ecosystems and Species	(C) Not reported	
EN28	IUCN (World Conservation Union) Red List Species	(C) Not reported	
EN29	Business Units in Sensitive Areas	(C) Not reported	
EN30	Other Relevant Indirect GHG Emissions	Part II - p. 68-69	
EN31	Basel Convention Waste	(C) Not reported	
EN32	Water Discharge/Runoff Effects	(C) Not reported	
EN33	Suppliers' Performance – Environmental Programs	Part II - p. 56-73	
EN34	Transportation/Logistics Environmental Impacts	Part II - p. 68-69	
EN35	Environmental Expenditures	(C) Not reported	
Social Performance Indicators: Labor Practices and Decent Work			
LA1	Workforce Breakdown	Part II - p. 3, (B)	
LA2	Employment Creation and Turnover	(D) Not reported	
LA3	Unionization/Employee Organization	Part II - p. 54	3
LA4	Restructuring Policies and Procedures - Employees	Part II - p. 54-55, (B)	3
LA5	Occupational Accidents and Diseases	(D) Not reported	
LA6	Health and Safety Committees	(D) Not reported	
LA7	Work-Related Injuries, Absenteeism and Fatalities	(D) Not reported	
LA8	HIV/AIDS Policies and Programs	(A) Not reported	
LA10	Equal Opportunity Policies, Programs and Monitoring Systems	Part II - p. 10, (B)	6

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GRI Indicator	Indicator Description	Section/Notes	Corresponding Global Compact Principle
LA11	Senior Management Diversity Measures	Part II - p. 54	6
LA12	Employee Benefits	Part II - p. 53	
LA13	Former Worker Representation	Part II - p. 54	
LA14	ILO Guidelines for Occupational Health Management Systems	(D) Not reported	
LA15	Health and Safety – Formal Agreements	(C) Not reported	
LA16	Continued Employability Programs	(A) Not reported	
LA17	Lifelong Learning Programs	(D) Not reported	
Social Performance Indicators: Human Rights			
HR1	Human Rights Policies and Procedures	Part II - p. 16	1
HR2	Human Rights – Supplier/Contractor Selection	Part II - p. 17-18	1, 2
HR3	Human Rights – Evaluation Methods/Monitoring Systems	Part II - p. 17-24	1, 2
HR4	Discrimination Prevention	Part II - p. 36	1, 6
HR5	Freedom of Association Policy	Part II - p. 36, 38-40	3
HR6	ILO Convention 138 – Child Labor Policy	Part II - p. 36, 46	5
HR7	Forced Labor	Part II - p. 36	4
HR8	Human Rights – Employee Training	Part II - p. 29-31	
HR9	Appeal Practices	Part II - p. 36, 41-42	
HR10	Non-Retaliation Policy/Employee Grievance System	Part II - p. 36, 41-42	
HR11	Human Rights – Security Personnel Training	(C) Not reported	
HR12	Indigenous People Policies	(C) Not reported	
HR13	Community Grievance Mechanisms	(C) Not reported	
HR14	Operating Revenues to Local Communities	(C) Not reported	
Social Performance Indicators: Society			
SO1	Community Impacts	Part II - p. 74-82	
SO2	Bribery and Corruption	Part II - p. 6	10
SO3	Political Lobbying and Contributions	Part II - p. 83-85	
SO4	Awards	Part II - p. 55, SRI p. 96	
SO5	Political Party/Candidate Contributions	Part II - p. 83	
SO6	Court Decisions – Antitrust	(C) Not reported	
SO7	Anticompetitive Behavior	Part II - p. 6	
Social Performance Indicators: Product Responsibility			
PR1	Customer Health and Safety	Part II - p. 5	
PR2	Product Information and Labeling	(D) Not reported	
PR3	Consumer Privacy	(C) Not reported	
PR4	Non-Compliance With Regulations	(C) Not reported	
PR5	Health and Safety-Related Complaints Upheld by Regulatory Body	(C) Not reported	
PR6	Voluntary Code Compliance	(C) Not reported	
PR7	Instances of Non-Compliance – Product Information and Labeling	(C) Not reported	
PR8	Customer Satisfaction	(C) Not reported	
PR9	Advertising – Adherence to Standards	(C) Not reported	
PR10	Advertising and Marketing Regulation Breaches	(C) Not reported	
PR11	Consumer Privacy – Breaches Complaints	(C) Not reported	

WEB LINKS

AccountAbility	www.accountability.org.uk
American Academy of Pediatrics	www.aap.org
American Chamber of Commerce, European Union	www.eucommittee.be
Beaverton Chamber of Commerce	www.beaverton.org
BRAC	www.brac.net
British Sports and Allied Industries Federation	www.rosl.org.uk/organisations.html
Business for Social Responsibility	www.bsr.org
Center for Energy and Climate Solutions	www.energyandclimate.org
Centers for Disease Control	www.cdc.gov
Ceres	www.ceres.org
CH2M Hill	www.ch2m.com
Citizenship CSR Consultancy	www.corporate-citizenship.co.uk
Council on Foreign Relations Corporate Program	www.cfr.org
Dow Jones Sustainability Index	www.sustainability-index.com
ECO Northwest	www.econw.com
Environmental Resource Trust	www.ert.net
Ethibel	www.ethibel.org
Ethical Trading Initiative	www.ethicaltrade.org
European American Industry Council	www.eabc.org
European Policy Centre	www.theepc.be
Fair Labor Association	www.fairlabor.org
Federation of European Sporting Goods Industry	www.fesi-sport.org
Footwear Distributors and Retailers of America	www.fdra.org
FTSE 4 Good	www.ftse.com/ftse4good/index.jsp
General Board of Pension and Health Benefits of the United Methodist Church	www.gbophb.org
Green Blue	www.green-blue.com
Global Reporting Initiative	www.globalreporting.org
Human Rights Campaign	www.hrc.org
International Center for Research on Women	www.icrw.org
International Labor Organization	www.ILO.org
International Youth Foundation	www.iyfnet.org
King Baudouin Foundation	www.kbs-frb.be
KLD Research and Analytics Inc	www.kld.com
Lance Armstrong Foundation	www.laf.org
Mercy Corps	www.mercycorps.org
Metafore	www.metafore.org
Minority Corporate Counsel Association	www.mcca.com
Minority or Women Owned Business Enterprises	www2.state.de.us
National Head Start Association	www.nhsa.org
National Industrial Transportation League	www.nitl.org
National Minority Supplier Diversity Council	www.nmsdcus.org
National Recycling Coalition	www.nrc-recycle.org
Opportunity International	www.opportunity.org
Oregon Association of Minority Entrepreneurs	www.oame.org
Oregon Business Association	www.oba-online.org
Oregon Business Council	www.orbusinesscouncil.org
Organic Exchange	www.organicexchange.org
Organic Trade Association	www.ota.com
Phylmar Consulting	www.phylmar.com

Population and Community Development Association	www.pda.or.th
Portland Business Alliance	www.portlandalliance.com
Retail Industry Leaders Association	www.retail-leaders.org
Shaping America's Youth	www.shapingamericasyouth
Society of Organizational Learning (SoL)	www.solonline.org
Sporting Goods Manufacturers Association	www.sgma.com
Stanford University's Positive Coaching Alliance	www.positivecoach.org
SustainAbility	www.sustainability.com
The Boys and Girls Clubs of America	www.bgca.org
The International Textile, Garment and Leather Workers' Federation	www.itglwf.org
The Natural Step	www.naturalstep.org
The Population Council	www.popcouncil.org
The World Bank	www.worldbank.org
UN Global Compact	www.unglobalcompact.org
United Nations Foundation	www.unfoundation.org
United Nations High Commission for Refugees	www.unhcr.ch
U.S. Chamber of Commerce	www.uschamber.com
U.S. Council for International Business	www.uscib.org/index.asp
U.S.-ASEAN Business Council	www.us-asean.org
U.S.-Vietnam Trade Council	www.usvtc.org
Waterfront Coalition (Washington, DC)	www.portmod.org
World Bank	www.worldbank.org
World Federation of Sporting Goods Industries	www.wfsgi.org
World Resource Institute	www.wri.org
World Trade Organization	www.wto.org
World Wildlife Fund	www.worldwildlife.org
YMCA	www.ymca.net
Youth Sport Trust	www.youthsporttrust.org

INDEX OF TERMS

CLS	Code Leadership Standard	PFP	Perfluoropropane
CO ₂	Carbon dioxide	PVC	Polyvinyl chloride
CR	Corporate responsibility	RSL	Restricted substances list
ESH	Environment, safety and health		MRS L Manufacturing restricted substances list
FOA	Freedom of association		PR SL Packaging restricted substances list
FY	Fiscal year	ROI	Return on investment
GHG	Greenhouse gas	SRI	Socially responsible investment / investor
MAP	Master Action Plan	SF ₆	Sulphur hexafluoride
MFA	Multi-Fiber Arrangement	SHAPE	Safety, Health, Attitude, People and Environment (audit tool)
NGO	Non-government organization	VOC	Volatile organic compound
NSAP	New Source Approval Process		

SOCIALLY RESPONSIBLE INVESTMENTS (SRI)

Nike is proud to be recognized by the following institutions, each of which helps investors gauge whether a specific company should be considered a socially responsible investment (SRI).



The FTSE4Good Index Series measures the performance of companies that meet globally recognized corporate responsibility standards, and facilitates investment in these companies. Listed companies must be working toward environmental sustainability, developing positive relationships with stakeholders, and upholding and supporting universal human rights.



The Ethibel Investment Register is the basis for SRI products for a growing number of European banks, fund managers and institutional investors. The Ethibel Sustainability Indexes combine a sound financial return with a positive impact on society to select the world's leading companies in terms of sustainability. The indexes contain the pioneer and best-in-class companies with respect to sustainability across sectors and regions in Europe, the Americas and the Asia-Pacific countries.



The Dow Jones Sustainability Indexes assess the opportunities and risks deriving from a company's economic, environmental and social developments, based on a defined set of criteria and weightings. They give asset managers reliable and objective benchmarks to manage sustainability portfolios. The indexes only select and rank companies that are among the sustainability leaders in their field (to review the DJSI assessment, see our website at <http://www.nikeresponsibility.com/reports>).

www.nikeresponsibility.com