

Procurement

In order to be able to produce our finished products, we need externally procured materials (raw materials, packaging, and traded goods) and services. These items all fall under the general category of **direct materials**. Examples include washing-active substances (surfactants), adhesive components, cardboard boxes or external filling services. The prices paid for total direct materials rose in 2011, stabilizing at a high level in the second half of the year.

In addition to the forces of supply and demand, the prices of raw materials, packaging, contract manufacturing and traded goods are essentially determined by the prices of the input materials used in their manufacture (feedstocks). And here we saw the extraordinary price fluctuations on the procurement markets of 2010 repeated through 2011. The price upsurge with respect to petrochemical products continued, extending to other feedstocks such as oleochemicals, paper and metals. The situation was exacerbated by supply shortages due to demand rising in the wake of expanding economic development. And there were disruptions in the supply chains of external vendors caused by postponed maintenance and repair activities, and unforeseen failures in production facilities. These developments led to feedstock price levels which, taking the average for the year, were substantially above the 2010 figure. A delayed increase in the purchase prices of the raw materials, packaging, contract manufacturing and traded goods procured by Henkel then ensued.

Our expenditures for total direct materials in the year under review amounted to 7.3 billion euros, 0.6 billion euros more than in the previous year. This is primarily attributable to higher production volumes and increased prices for feedstocks. Through our global procurement strategy, we were able to cushion the effect on adjusted¹ gross margin exerted by the price increases for our direct materials. However, we were unable to compensate for them fully.

In order to improve efficiency and secure material supplies, we consistently endeavor to optimize our value chain while maintaining quality levels. In addition to our diligence in negotiating new, competitive contractual conditions, our ongoing global program aligned to reducing overall procurement cost is a major factor in the success of

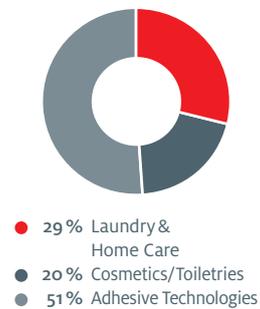
our purchasing strategy. Working together with the three business sectors, Purchasing is permanently engaged in reducing product complexity, optimizing our raw material mix and promoting the standardization of packaging and raw materials. This gives us stronger negotiating positions and creates scope for further consolidation of our vendor base. In establishing long-term business relationships, we focus our efforts on vendors in which we see potential with respect to innovation, optimization of manufacturing cost and improving our logistics processes. One of our main concerns within this context is to limit the risk of supply shortages. We manage our preferred vendors on the basis of individual target agreements. Through these measures, we have succeeded in reducing the number of vendors we use by 10 percent.

We have been able to increase the processing and management efficiency of our purchasing activities by further standardizing, automating and centralizing our procurement processes. Large parts of our administrative work, for example purchase order processing and price management, have been pooled within our shared service center organization.

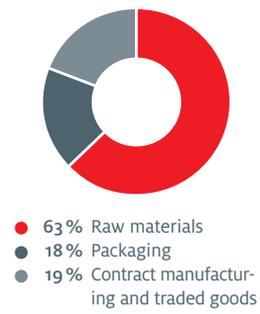
The improvement in our net working capital is due particularly to the optimization of our terms and conditions of payment with respect to our suppliers. We have also succeeded in optimizing our raw material inventories through a process of continuous improvement in our supply chain processes.

Given the uncertainties that exist with respect to material price development and supply shortages on the procurement markets, risk management constitutes an important aspect of our purchasing strategy, with the emphasis on reducing price and supply risks while maintaining uniformly high quality. In adopting an active price management approach, we deploy strategies aligned to safeguarding prices over the long term, both through contracts and – where appropriate and possible – by means of financial hedging instruments. In order to minimize the risks of delivery default, we put in place supply disruption clauses and perform detailed risk assessments of our vendors to determine their financial stability. With the aid of an external, independent financial services provider, we continuously monitor important suppliers whose financial situation is regarded as critical. If a high risk of vendor

Material expenditures by business sector



Material expenditures by type



¹ Adjusted for one-time charges/gains and restructuring charges.

failure is identified, we systematically prepare back-up plans in order to ensure consistency of supply.

We expect our suppliers and contractual partners to behave in a manner in keeping with our own corporate ethics and values. The basic requirements in this regard are set out in our purchasing standards, valid across the Group, and our safety, health and environmental standards formulated in 1997, through which we have long acknowledged our responsibility for the entire supply chain. Consequently, when selecting and developing our vendors and contractual partners, we also consider their performance in relation to the requirements of sustainable development. We use the cross-industry Code of Conduct published by the German Federal Association of Materials Management, Purchasing and Logistics [BME] as a globally applicable vendor code and the basis for our multi-faceted "Responsible Supply Chain Process." The objective of this process is to ensure compliance by our suppliers with these standards and to improve, together with our strategic vendors, the sustainability standards pertaining to our supply chain. A global training program further ensures that the requirements governing the sustainability profile of our vendors are understood and properly applied by our employees.

Our five most important commodity groups are raw materials for use in hotmelt adhesives, washing-active substances (surfactants), raw materials for polyurethane-based adhesives, solvents and inorganic raw materials for use e.g. in detergents and surface treatment products. These account for around 34 percent of our total direct material expenditures. Our five largest suppliers account for around 14 percent of our direct material cost.

Purchases made in the general category **indirect materials and services** are not directly linked to the production of our finished products. Examples include maintenance, repair and overhaul materials, and logistics, marketing and IT services. Through our global procurement strategy and structural cost reduction measures, we succeeded in reducing our procurement prices in these categories compared to the previous year.

Due to positive business developments, the overall volume of indirect materials and services rose in 2011. The related expenditures therefore increased compared to 2010, by 0.4 billion euros to 4.3 billion euros.

Production

We further optimized our production footprint in 2011, with Henkel manufacturing products with a total weight of around 7.6 million metric tons at 180 sites located in 56 countries around the world. Our largest production facility is in Düsseldorf, Germany. Here we manufacture not only detergents and household cleaners but also adhesives for consumers and craftsmen, and products for our industrial customers. Cooperation with toll manufacturers is an integral component of our production strategy, enabling us to optimize our production and logistics structures when developing new markets or where volumes are still small. Each year we purchase around 10 percent in additional production tonnage from toll manufacturers based on current figures.

Number of production sites

	2010	2011
Laundry & Home Care	31	29
Cosmetics/Toiletries	8	8
Adhesive Technologies	149	143
Total	188	180

Our Düsseldorf facility is also the largest production site of the **Laundry & Home Care** business sector. Here we predominantly manufacture powder and liquid detergents, fabric softeners and liquid cleaning products. We have further upgraded our Germany-based production activities within our European manufacturing concept. Following the construction of a factory in Düsseldorf for the production of liquid laundry and home care detergents in 2010, we have now also constructed on the same site a new facility for the manufacture of machine-dishwashing tabs to be supplied to the markets of Germany, the rest of Europe and the Middle East region as from 2012.

In 2011, we further reduced the number of production sites around the world from 31 to 29. Concentrating our laundry and home care product