Gap Inc.

SOCIAL RESPONSIBILITY REPORT

"This report contains a great deal of information that many companies have not provided publicly, and includes valuable insights from a company that we believe is sincerely struggling with these complex issues."

Public Reporting Working Group:

Adam Kanzer, Esq., Domini Social Investments LLC

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David M. Schilling, Interfaith Center on Corporate Responsibility

For the full text of the Public Reporting Working Group's statement regarding this report, please see Page 28.

Main cover photo: Xiuxia, 26, works in the inspection department of a Gap Inc.-approved garment factory in southern China. The factory is one of approximately 241 Gap Inc.- approved facilities in China.

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Period covered: Unless otherwise noted, all references to 2003 are for the calendar year, not Gap Inc.'s fiscal year, which ended January 31, 2004.

Paul Pressler
President and Chief Executive Officer

Executive Summary

When I decided to join Gap Inc. in the fall of 2002, one of the first things my teenage daughter asked was, "Doesn't Gap use sweatshops?" I was able to tell her how the company was working to fight sweatshop practices and improve garment factory conditions around the world.

Her question didn't surprise me, though. Our company hasn't done enough to tell people about our efforts. We have an opportunity to improve our transparency and better communicate with our employees, shareholders and other concerned stakeholders. This social responsibility report, our company's first, is a big step toward that goal. For several years, we have provided an overview of our ethical sourcing practices on our company's Web site, gapinc.com. This report, also available online, discusses our efforts more thoroughly. It provides comprehensive monitoring data about factory conditions and greater insights into the complex challenges we face, our collaborations with stakeholders worldwide and the longer-term solutions we believe are necessary to achieve lasting change in the garment industry.

We believe that garment and other manufacturing workers around the world deserve better than the reality that many unfortunately face. We recognize and embrace our duty to take a leadership role. While we know firsthand that positive change is possible, we also have learned that creating sustainable and scalable solutions across the retail apparel and garment manufacturing industries is immensely difficult. We are working to effect change in factories that produce apparel for many apparel retailers. And while some of these retailers share our commitment, others may not.

More collaboration is needed. To foster greater compliance with labor standards in garment factories, we support multi-stakeholder efforts currently under way to develop a universal code adopted and enforced by all apparel brands and retailers. We would endorse a universal code that is at least as stringent as our current standards, including a commitment to freedom of association, and that is consistent with the International Labour Organization's (ILO) core labor standards. We believe a strong universal code, with consistent enforcement by all apparel brands and retailers, will promote more collaboration and result in more effective use of industry monitoring and compliance resources.

Capacity building is another issue important to us. Improving one factory is challenging enough. Creating sustainable change across a country or region often seems impossible. In many countries, governments simply don't have the resources or the will to enforce laws and regulations. Non-governmental organizations (NGOs) struggle to develop the skills and find the financial resources necessary to support meaningful change on a broader scale. Retailers, manufacturers, governments, unions and NGOs must work together more

Improving garment factory conditions is a central element of our overall commitment to social responsibility, which is why we've made this work the primary focus of our first report. But our social responsibility commitments don't stop there. Community giving and volunteerism also are deeply embedded in our company's culture and values, as well as a commitment to the environment, to strong corporate governance and ethical business practices, and to making sure we're continually developing and supporting our more than 150,000 employees worldwide.

effectively to create a stronger framework. To that end, we are working with partners worldwide to complement our efforts. As international trade agreements are negotiated, we're supportive of additional efforts to strengthen compliance with national laws and international labor standards. We continually work to encourage greater ownership and responsibility by garment manufacturers for conditions in their factories.

We are convinced that collaborative, multi-stakeholder engagement is the only way to create sustainable change industrywide. That's why we've been expanding our global partnerships and significantly broadening our work with outside groups. For example, we recently joined Social Accountability International's (SAI) Corporate Involvement Program, the Ethical Trading Initiative (ETI) and the United Nations' Global Compact.

We're constantly learning how to work smarter and more effectively. We've been evolving our program since the early 1990s, when we first developed labor guidelines for garment manufacturers. In 1996, we developed a more comprehensive Code of Vendor Conduct. The code clearly prohibits child labor, forced labor and discrimination, and protects freedom of association and other rights for workers.

We have a comprehensive internal monitoring program. Today we have a global network of more than 90 full-time employees who hold garment manufacturers accountable for respecting workers' rights and providing acceptable conditions. Our compliance team embodies our commitment to socially responsible and ethical business practices.

The goal is not only to improve ongoing compliance with our standards, but also to show factories what success looks like and how operating in a socially responsible way can improve their business. When problems are found, our team works with garment manufacturers to fix them. In doing so, we try to build trust and create an environment that fosters continual improvement.

We know that if we were to pull out of a factory every time a problem was found, management might feel inclined to hide violations rather than work with us, and issues would never be resolved. Workers' jobs also may be put at risk. However, sometimes we have no choice. If garment manufacturers refuse to work with us, we won't keep working with them. When serious or excessive problems are discovered and remain uncorrected, we often make the difficult decision to leave.

Executive Summary

We are convinced that collaborative, multi-stakeholder engagement is the only way to create sustainable change industrywide. That's why we've been expanding our global partnerships and significantly broadening our work with outside groups.

In 2003, we revoked the approval of 136 factories. Sometimes, garment manufacturers also stop doing business with us because they believe our standards are too stringent.

To complement our internal compliance efforts we have been a leader in supporting independent monitoring in Central America and elsewhere, and sponsoring supervisor and worker training initiatives such as the Cambodian Labor Training Coalition. These third-party initiatives are an important part of our program. In this report, four case studies, focusing on Central America, Lesotho, Cambodia and China, illustrate the complexities of creating sustainable improvements. Also included is stakeholder feedback we've received on what we do well and what we can do better, from groups such as the Maquila Solidarity Network (MSN).

Improving garment factory conditions is a central element of our overall commitment to social responsibility, which is why we've made this work the primary focus of our first report. But our social responsibility commitments don't stop there. Community giving and volunteerism also are deeply embedded in our company's culture and values, as well as a commitment to the environment, to strong corporate governance and ethical business practices, and to making sure we're continually developing and supporting our more than 150,000 employees worldwide. These efforts also are highlighted in this report.

Our Board of Directors strives to maintain the highest ethics and integrity in every aspect of our business. Independent directors comprise our Governance, Nominating and Social Responsibility Committee, which oversees our corporate governance and social responsibility practices. Independent directors also represent a majority of our Board.

Giving back to our communities is a vital part of our culture. In 2003, Gap Inc. employees volunteered nearly 22,000 hours through company-sponsored programs. We cleaned community parks and restored creek habitats, helped kids with art projects and fed the homeless. In December 2003, our employees in the United States and Canada adopted more than 1,000 families for

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the holidays and ensured that they received gifts on their wish lists. Throughout the year, we support volunteerism by providing full-time employees the opportunity to take paid time off for volunteer activities. Through our "Money for Time" program, we donate $150 for every 15 hours an employee volunteers to a community organization.

Through our Gap Foundation, we've donated approximately $60 million in grants during the past five years, or approximately one percent of net earnings before taxes for the period, to organizations worldwide that are focused on helping children, youth and families. In the United States, our Foundation has provided national support to Boys & Girls Clubs of America and to the Lorraine Monroe Leadership Institute, which provides training to public school principals. We also make substantial product donations (more than $12 million in 2003, for example) to organizations that help people in need. Product donations and employee volunteerism significantly extend our financial support to communities in which we live, work and do business.

As we continue to evolve in our social responsibility efforts, we are committed to communicating our progress and challenges, and soliciting ongoing feedback from our employees, shareholders and other concerned stakeholders. We want to hear from you. A feedback form is included in this report. You also can email us at social_responsibility@gap.com.

I am proud of the passion and dedication of our employees worldwide. Every day, they honor the values of this company and exemplify our belief in doing business in a socially responsible way. We've accomplished a lot, as shown in this report, but there's always more we can learn and do. How we do business is as important to us as what we do—and we'll continue working hard to ensure that our actions consistently support our values. ■

Anne Gust
Executive Vice President,
Chief Administrative and Compliance Officer

Developing Our Program

Conducting our business with integrity is a core value of Gap Inc. As the company's Chief Administrative and Compliance Officer, a big part of my job is ensuring that we live up to that value every day. My team is responsible for making sure our ethics policies are more than just words on paper. Our codes of conduct, whether for garment manufacturers or for our own employees, reflect how we run our business. Both our CEO and Board of Directors hold my group accountable for making sure Gap Inc. operates in a socially responsible way.

Members of my team are responsible for most of the areas covered in this report, from environmental policies and community involvement to corporate governance and global garment manufacturer compliance. We work to make sure our policies are embedded in all of our business practices.

Although only one aspect of our broader commitment to social responsibility, we have focused most of this report on our ongoing efforts to achieve sustainable and measurable improvements in garment factory conditions and labor standards.

Since the early 1990s, when Gap Inc. and a few other companies in our industry began to focus on working conditions in the global garment industry, we have greatly evolved our approach to this issue. We started with a strong foundation—our Code of Vendor Conduct—which is based on internationally accepted labor standards and is published in 24 languages. It lays out our operating requirements for any garment manufacturer that wants our business. No garment manufacturer or factory is in full compliance with all requirements all of the time. But our expectations for continuous improvement are clear. Our code's eight key sections are highlighted on this page.

Our Code

Gap Inc.'s Code of Vendor Conduct consists of eight major areas:

- Local labor laws
- Environmental
- Discrimination
- Forced labor
- Child labor
- Wage and hour requirements
- Working conditions
- Freedom of association

For the complete Code of Vendor Conduct, visit us at gapinc.com.

We believe our program has helped improve conditions in the factories that make our apparel. Our focus now is to help foster more sustainable solutions across the industry. Our challenge is to determine how best to work with stakeholders, including NGOs, unions, governments and other apparel brands and retailers, to move garment manufacturers toward global and sustainable improvements in labor standards. These efforts will create a stronger framework to more consistently enforce labor standards among all garment factories and help drive greater ownership of labor standards by manufacturers.

The information on Page 7 shows how our program has evolved and how we rate ourselves today against our objectives. Continuous improvement is important to us and to many of our stakeholders. This report demonstrates our strengths and opportunities, and our desire to more fully engage stakeholders while addressing challenges and creating global, industrywide capabilities to achieve lasting improvements.

EVOLVING OUR PROGRAM & DEVELOPING OBJECTIVES

Gap Inc. began addressing conditions in third-party garment manufacturers in 1992, with the development of our first set of labor, health and safety standards for manufacturers. Since that time, we have steadily evolved our program, as the chart below illustrates. Our standards, as detailed in our Code of Vendor Conduct, form the foundation of our efforts and set clear expectations for the garment manufacturers that produce our merchandise. We enforce those standards through a comprehensive global monitoring program. In the past few years, we have begun to broaden our focus beyond monitoring, recognizing the need for broader stakeholder engagement and capacity building to more fully address issues in the garment industry longer term.

We believe these efforts, coupled with our ongoing monitoring, will help create and support more sustainable solutions. Critical to this goal is continuing to drive greater ownership by garment manufacturers of labor, health and safety standards in their own factories, rather than having standards imposed by apparel brands and retailers. Capacity building efforts with governments, NGOs and civil societies worldwide is important in ensuring that comprehensive frameworks exist to support and enforce internationally recognized standards.

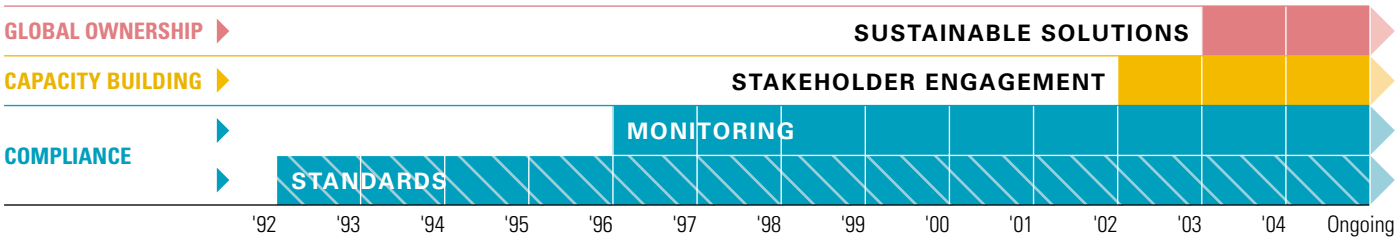
GAP INC. SELF-ASSESSMENT AGAINST OBJECTIVES

Supplier monitoring for compliance with company standards	SIGNIFICANT PROGRESS
Supply chain alignment with CSR practices	OPPORTUNITY
External engagement with NGOs/stakeholders	SIGNIFICANT PROGRESS
Transparency	OPPORTUNITY
Industry collaboration	OPPORTUNITY
Public policy engagement	SIGNIFICANT PROGRESS

Assessing our own performance against our objectives (illustrated above), we believe our record demonstrates leadership in monitoring garment factory conditions and enforcing established standards. In other key areas, such as external stakeholder engagement and public policy engagement, we believe our efforts show progress against our objectives. At the same time, we believe we have more work to do to establish leadership in the areas of supply chain alignment, transparency and industry collaboration.

Our efforts are described in detail in this, our first report, and represent our commitment to greater transparency. Additional information can be found at gapinc.com.

EVOLUTION OF OUR EFFORTS TO IMPROVE GARMENT FACTORY CONDITIONS



Our Program Today

GLOBAL COMPLIANCE EVOLUTION

YEAR	MILESTONE
1992	Gap Inc. develops Sourcing Guidelines outlining general labor standards for vendors to follow; Quality Assurance employees oversee this initiative.
1995	Labor conflict at Mandarin International factory in El Salvador (see Page 20) increases company's awareness of factory conditions and the need to ensure vendor commitment to Sourcing Guidelines.
1996	In the wake of Mandarin incident, Gap Inc. partners with three outside organizations to form the Independent Monitoring Working Group, which pioneers the industry's first independent monitoring program in El Salvador. Gap Inc. forms internal compliance organization, hiring first Vendor Compliance Officers, and begins to separate compliance from Quality Assurance function. Sourcing Guidelines replaced by comprehensive Code of Vendor Conduct.
1999	Gap Inc. is one of many apparel retailers named in Saipan lawsuit (see Page 9), an experience that highlights the need to refine and better articulate requirements for foreign contract garment workers. To further strengthen compliance function, Gap Inc. separates compliance from sourcing, establishing independent Global Compliance department reporting into company's Chief Administrative and Compliance Officer.
2000	Journalist alleges child labor violations at Cambodian garment factory; Gap Inc. requires additional age verification in that country (see Page 24). Gap Inc. becomes second corporate partner of Global Alliance as part of multiyear commitment to identify garment worker needs, develop training for workers and management and provide community-based services.
2001	Gap Inc. implements guidelines to help protect rights of foreign contract garment workers, including freedom to return to their home country (see Page 9).
2002	Gap Inc. supports formation of Public Reporting Working Group (see Page 28). Gap Inc. pilots program to rate factory compliance (see Page 16). Global Partnerships group formed within Global Compliance department to focus on stakeholder dialogue and engagement. Gap Inc. supports Cambodian Labor Training Coalition on an initiative to improve factory conditions and relations between workers and management (see Page 25).
2003	Gap Inc. strengthens external engagement by joining SAI's Corporate Involvement Program and the United Nations' Global Compact (in April 2004, Gap Inc. joined ETI).

More than 90 full-time employees work in Global Compliance. Most are Vendor Compliance Officers (VCOs) who work to improve labor conditions among the garment manufacturers that produce our apparel and operate approximately 3,000 garment factories in about 50 countries.

Most VCOs are from the region or country they oversee. They represent about 25 nationalities and speak as many languages. Some have worked in factories as managers or on the production line. Others have experience in education and government or with NGOs. Still others were local labor organizers or lawyers. We believe this diversity and localized approach greatly enhances the team's commitment and effectiveness. A profile of one of our VCOs, VannChhai Leng, is included with the Cambodia case study on Page 25. Other profiles can be found at gapinc.com.

OUR PROGRAM SCOPE

Headed by Dan Henkle, Vice President of Global Compliance, our Global Compliance department is separate from and independent of our sourcing organization and focuses on improving factory working conditions and labor standards.

While factory monitoring is an important part of our program, we know that it isn't enough to support sustainable change. Most garment manufacturers work with many customers. Our influence on a given manufacturer's practices is limited when we represent only a fraction of its production. So, in 2002, we initiated a strategy to collaborate with partners worldwide in an effort to foster longer-term solutions.

"There are no easy answers to complex problems. Monitoring helps, but sustainable change across our industry will only occur through collaboration with partners worldwide."
Dan Henkle, Vice President of Global Compliance

Because NGOs often have close relationships with garment workers, they are able to provide us with insights into factory conditions that our compliance team may not see. By working more closely together, we've found that we are often able to resolve issues before they escalate into a crisis. Such partnerships also give us the chance to address broader issues, from a variety of perspectives.

To date, we've engaged with three types of organizations:

• Multi-stakeholder groups such as SAI, ETI, and the Global Alliance for Workers and Communities (GA), where we work with other companies and organizations on shared concerns.

• Groups with global reach, such as MSN and Union of Needletrades, Industrial and Textile Employees (UNITE), which provide us with critical information and expertise as exemplified in the Lesotho case study on Page 22.

• Local groups, such as the Cambodian Labor Training Coalition (see Page 25), which address country-specific challenges.

A number of stakeholders have commented on our efforts, highlighting what we do well and what we can do better (see Page 18). In particular, the five organizations we've partnered with to form our Public Reporting Working Group—Domini Social Investments, the Calvert Group, the As You Sow Foundation, the Center for Reflection, Education and Action (CREA), and the Interfaith Center on Corporate Responsibility (ICCR)—have provided their views on this report and our progress toward transparency (see Page 28). ■

Protecting Foreign Contract Workers

In January 1999, a U.S. federal class-action lawsuit was filed against 18 apparel retailers, including Gap Inc., that purchased merchandise made in Saipan, part of the U.S. Commonwealth of the Marianas Islands. Almost every garment manufacturer on the island also was sued. The lawsuit alleged poor factory conditions and mistreatment of immigrant workers who came from China, the Philippines and other countries after signing employment contracts for jobs on Saipan.

We vigorously defended ourselves because we felt strongly that the allegations against us were untrue. The lawsuit treated all retailers and manufacturers the same, regardless of specific factory conditions and company practices. We had production in only a small number of the factories sued, and we monitored those factories on an ongoing basis. In September 2002, we entered into a settlement. The agreement benefited all parties by establishing Saipan's first independent factory monitoring program.

The lawsuit increased our awareness about "foreign contract" workers and the unique vulnerabilities they face at the hands of recruitment agents and factory management. To obtain a job, these workers typically incur debt that must be repaid before they can return home.

In 2001, we implemented strict guidelines to better protect foreign contract workers in the approximately five percent of Gap Inc.-approved factories that employ them worldwide. Employment contracts must be written in the workers' native languages and workers must be paid at least the local minimum wage. Factory management must allow workers to control their own travel documents and wages. Most importantly, workers must be free to leave the factory and return home at any time and management must agree to assume a proportionate amount of the returning workers' debt. ■

Manufacturer and Factory Approval Process

Our initial factory evaluation process is a cornerstone of our program. Before any order is placed, we must evaluate and approve the manufacturer and each garment factory it intends to use for our production.

The initial evaluation process applies to all garment manufacturers, their factories and subcontractors. Our sourcing team assesses factories before an approval request is sent to Global Compliance. Approval involves a multi-step qualification process, outlined below. The process can take from a week to more than a year to complete. Approximately 90 percent of the factories we evaluate fail the initial inspection. While most factories correct problems and are eventually approved, we ultimately reject about 16 percent of all new factories evaluated.

No garment factory is perfect. But this process helps ensure that we screen out the worst factories and look for those that have the ability to meet our standards, provide decent conditions and treat workers fairly. While we strive to help approved factories make ongoing improvements, some factories consistently fail to live up to their commitments.

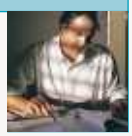
Our approval process involves three steps:
1) **A manufacturer's written commitment:** A manufacturer must sign our compliance agreement, stating its commitment to abide by our Code of Vendor Conduct. The manufacturer is required to provide a profile of each facility it plans to use for our order and its workers. The manufacturer also must agree to allow us unrestricted access to factory workers, working and living facilities and employment records. Manufacturers sometimes remove themselves, or we may remove them, from consideration at this stage because they either cannot, or will not, meet our standards.

2) **Our initial evaluation visit:** Once the required paperwork has been reviewed, a VCO schedules a visit. A detailed assessment of factory conditions is conducted based on the eight sections of our code. Any violations are documented. Our policy is that no garment factory is approved without an inspection by one of our VCOs.

The Approval Process in Action:

Our approval process can take from one week to more than a year to complete. This timeline shows an actual approval process in the second half of 2003 for a new factory in Guatemala. In this example, the process took just under four months.

7/15/03	7/24/03	8/07/03	8/08/03
REQUEST	**DOCUMENTATION**		**EVALUATION**
Gap Inc.'s regional sourcing office in Miami requests that our compliance team evaluate a new factory in Guatemala for approval.	Compliance staff sends required documents to factory.	Factory management submits completed documents.	VCO based in Guatemala schedules a factory visit.



2003 FACTORY APPROVAL DATA

REGION*	NUMBER OF FULL-TIME GLOBAL COMPLIANCE EMPLOYEES	NUMBER OF NEW GARMENT FACILITIES EVALUATED	APPROVED	NOT APPROVED	PENDING
Greater China	17	101	80%	15%	5%
North Asia	6	36	94	3	3
Southeast Asia	18	118	84	8	8
Indian Sub-Continent	12	101	76	18	6
Persian Gulf	0	4	100	0	0
North Africa & the Middle East	2	40	50	25	25
Sub-Saharan Africa	4	40	60	18	22
Europe (including Russia)	5	99	66	26	8
United States & Canada	19**	23	83	4	13
Mexico, Central America & the Caribbean	9	67	81	15	4
South America	1	24	58	21	21
Total	**93**	**653**	**75%**	**16%**	**9%**

*For a list of countries in each region, please see the inside back cover of this report. **Includes headquarters staff based in San Francisco.

3) **A decision by our compliance team:** After analyzing the paperwork and the results of the evaluation, our Global Compliance staff determines whether the manufacturer is able to comply with our code. At this point, the manufacturer and applicable factories may be approved—meaning orders can be placed—or additional corrective action may be required. Follow-up evaluations may be needed. If a manufacturer does not satisfactorily correct the problems, or is unable or unwilling to make necessary changes, it will be rejected. Approved garment factories are then monitored on an ongoing basis. ■

9/17/03 — EVALUATION

VCO conducts initial evaluation of the factory.

9/19/03

VCO notifies management of corrective actions required to gain approval, which include installing a ventilation system in the spot cleaning area and providing workers with appropriate personal protective equipment for handling chemicals.

10/07/03

VCO conducts a follow-up visit to check status of requested changes and provides further feedback to factory management.

10/31/03

VCO conducts a third visit and confirms that all issues are resolved. Evaluation is submitted to Global Compliance administration staff.

11/04/03 — DECISION

Factory is approved and "activated," making it eligible to receive Gap Inc. orders.

Ongoing Factory Monitoring

We strive to monitor all approved garment factories at least once in a 12-month period. In 2003, our VCOs conducted approximately 8,500 visits to garment factories around the world. The chart at the right shows the percentage of factories visited in each region, both for those that were on our approved list for all of 2003 and those that were approved for any part of the year. The percentages in the second column are lower than in the first column as some facilities are removed from our approved list during the year before a visit can be conducted.

We monitor garment manufacturers and factories for their compliance with the eight main sections of our Code of Vendor Conduct. The chart on Pages 14-15 shows the regional distribution and the extent of verified code violations in 2003.

Few factories, if any, are in full compliance all of the time. If they were, we wouldn't need a code or the extensive resources we devote to monitoring. When we find problems, we work with management to try to resolve them as quickly as possible. We will stay with a manufacturer as long as we believe it is committed to making ongoing improvements.

Any violation concerns us, but we pay particular attention to violations of core areas of our code, including serious issues such as forced or child labor. We also take note when violations occur frequently, such as in the area of health and safety, or if we see a pattern develop over time. In 2003, we terminated our business with 136 factories for serious or excessive breaches of our Code of Vendor Conduct.

2003 FACTORY MONITORING DATA

	APPROVED FOR ALL OF 2003		APPROVED FOR ALL OR PART OF 2003	
REGION*	NUMBER OF GARMENT FACILITIES	PERCENT OF FACILITIES VISITED	NUMBER OF GARMENT FACILITIES	PERCENT OF FACILITIES VISITED
Greater China	252	100%	464	89%
North Asia	100	100	200	95
Southeast Asia	425	99	672	90
Indian Sub-Continent	370	96	592	90
Persian Gulf	22	91	42	83
North Africa & the Middle East	41	83	91	66
Sub-Saharan Africa	59	95	118	75
Europe (including Russia)	130	78	277	77
United States & Canada	104	80	188	70
Mexico, Central America & the Caribbean	143	94	298	87
South America	44	91	68	90
Total	1,690	94%**	3,010	86%**

* For a list of countries in each region, please see the inside back cover of this report.
** A number of factors, including staffing and limited transportation to remote regions, prevented some facility visits in 2003.

CORE VIOLATIONS

While we consider all areas of our code important, there are core aspects of it that significantly impact working conditions. These range from wage and hour issues, such as correct payment of wages, voluntary overtime and at least one day off in seven, to our prohibition of forced labor, child labor and physical abuse and a worker's right to freedom of association.

We monitor core areas through a visual inspection of the factory, a thorough review of timecard, production and payroll records and by talking with workers. When violations are found, our VCOs work with management and sometimes workers to design and implement remediation plans. If we find that wages or overtime rates have not been paid in full, we typically require the factory to provide workers with back pay.

Violations in some core areas, such as freedom of association and discrimination, can be especially difficult to uncover and prove. When we investigate complaints, we often find ourselves grappling with different perspectives and conflicting views. Because allegations often involve disputes between workers and management, there are usually two or more sides to the story. Although our data in these areas for 2003 shows only a few verified cases, we believe violations were more widespread than our data suggests. We are currently working with our VCOs and external stakeholders to make our monitoring more effective in these areas.

A single serious violation—such as forced or child labor or knowingly falsifying records—threatens our relationship with a manufacturer. In 2003, we verified two instances of underage workers. In one case, the worker was considered underage because she was a few weeks shy of her sixteenth birthday, the minimum working age in that country. In the other, the worker was not properly registered with local authorities as a "young worker." We terminated business with both factories.

FREQUENT VIOLATIONS

Some code violations, such as in the area of health and safety, tend to occur frequently. This is, in part, because they are often temporary—an aisle blocked by a moveable cart, for example—and, in part, because they are easier for our monitors to spot during a factory inspection. Although such violations vary in severity, most are addressed quickly. As we work with manufacturers over time, we tend to see significant improvement in this area.

Violations of local law also tend to occur often. Sometimes this is because laws are unclear or contradictory, making compliance difficult. In other cases, government enforcement is insufficient or nonexistent. In still others, local regulations may not be publicized and manufacturers are unaware that the law even exists. To address this, our VCOs work to maintain a list of relevant local laws for the areas they monitor. However, given the complexity of the legal landscape and lack of transparency in some countries, this remains an ongoing challenge.

HABITUAL VIOLATIONS

Our goal is to help manufacturers improve their overall level of compliance over time. As a result, we pay attention not only to the type and frequency of violations, but also to the patterns in which they occur. We become concerned when we see the same violation occur over and over again, as it suggests either a lack of commitment on the part of management or a deeper systemic problem. To address these types of issues, we've begun to introduce training programs and other projects designed to target the root causes of problems. The four case studies on Pages 20-27 describe some of our efforts. ■

Our Code of Vendor Conduct outlines eight categories of labor and operating standards. All new garment manufacturers must be pre-approved before orders are placed. Once approved, factories are monitored on an ongoing basis. The chart below illustrates the regional distribution and frequency of code violations documented by Gap Inc. VCOs in approved factories in 2003.

2003 Code Violations

REGION*	GREATER CHINA	NORTH ASIA	SOUTHEAST ASIA	INDIAN SUB-CONTINENT	PERSIAN GULF	NORTH AFRICA & MIDDLE EAST	SUB-SAHARAN AFRICA	EUROPE (INCLUDING RUSSIA)	U.S. & CANADA	MEXICO, CENTRAL AMERICA & THE CARIBBEAN	SOUTH AMERICA
No. of active factories	464	200	671	592	42	91	118	277	188	298	68
No. of factories revoked for compliance violations	42	1	42	31	6	1	4	9	0	0	0
GENERAL PRINCIPLE											
Lacks full compliance with local laws											
Restricted access of Gap Inc. representatives											
ENVIRONMENT											
Lack of environmental management system or plan											
Insufficient notification procedures in case of environmental emergency											
DISCRIMINATION**											
Employment											
Wages & benefits											
FORCED LABOR											
Use of any kind of involuntary labor, including prison labor, debt bondage or forced labor											
For foreign contract workers, non-payment of agency recruitment fees and/or requiring workers to remain in employment against their will											
CHILD LABOR											
Workers are not 14 years old or do not meet minimum legal age requirement											
Not in full compliance with child labor laws											
Failure to allow eligible workers to attend night classes and/or participate in educational programs											
Poor age documentation											
WAGES & HOURS											
Pay is below minimum wage											
Overtime pay rates are below legal minimum											
Work week in excess of 60 hours											
Workers cannot refuse overtime without threat of penalty or punishment											
Workers do not have at least 1 day off in 7											
Violation of local laws on annual leave and/or holidays											
Unclear wage statements											

*For a list of countries in each region, please see the inside back cover of this report.

LEGEND

- No code violations verified
- Violations verified in less than 1% of factories
- Violations verified in between 1% and less than 10% of factories
- Violations verified in between 10% and less than 25% of factories
- Violations verified in between 25% and less than 50% of factories
- Violations verified in more than 50% of factories

REGION*	GREATER CHINA	NORTH ASIA	SOUTHEAST ASIA	INDIAN SUB-CONTINENT	PERSIAN GULF	NORTH AFRICA & MIDDLE EAST	SUB-SAHARAN AFRICA	EUROPE (INCLUDING RUSSIA)	U.S. & CANADA	MEXICO, CENTRAL AMERICA & THE CARIBBEAN	SOUTH AMERICA
WORKING CONDITIONS											
Physical punishment or coercion											
Psychological coercion and/or verbal abuse											
Violation of local laws on working conditions											
Insufficient lighting											
Poor ventilation											
Insufficient or poorly marked exits											
Obstructed aisles, exits or stairwells											
Locked or inaccessible doors and exits											
Insufficient number of and/or inadequately maintained fire extinguishers											
Insufficient number of fire alarms and/or emergency lights											
Not enough evacuation drills											
Machinery lacks some operational safety devices											
Inadequate personal protective equipment											
Insufficient access to potable water											
Inadequate first-aid kits											
Unsanitary toilets and/or restricted access											
Inadequate storage of hazardous and combustible materials											
FREEDOM OF ASSOCIATION* **											
Workers are not free to choose whether or not to lawfully organize and join associations											
Penalization or interference with workers' lawful efforts to organize											

General Principle—Lack of knowledge about, and compliance with, local laws is a common issue worldwide (see Page 13).

Environment—Common violations included inadequate environmental plans and documentation.

Discrimination—We believe violations in this area are more widespread than this data suggests. Examples of verified violations included a stated preference for female workers, wrongful termination of pregnant employees, pregnancy testing, inadequate hiring policies and procedures, and higher wages paid to local workers versus foreign workers.

Forced Labor—We verified one technical violation involving a contractual provision that required workers to remain employed at the factory for a minimum period following overseas skills training. This category includes an additional sub-set of provisions (not shown) specific to foreign contract workers (see Page 9).

Child Labor—We require manufacturers to ensure that workers are at least 14, the minimum age under our code, or the minimum working age allowed in the country, whichever is higher. In the two verified cases of child labor violations in 2003, both workers were older than 14, but one was younger than the country's legal minimum age and one was not properly registered as a "young worker." We terminated business with both factories.

Wages & Hours—Inaccurate recordkeeping, incorrect or non-payment of wages and excessive overtime hours are common violations. We regularly review timecard, payroll and production records and verify their accuracy through worker interviews. When violations are discovered, we typically require back-payment of wages as appropriate.

Working Conditions—While outright physical punishment and psychological coercion is rare, examples of violations verified by our team included verbal harassment by supervisors, factory regulations permitting physical labor as a disciplinary measure (such as sweeping floors), failure to display clear and fair disciplinary procedures and coaching of workers prior to a VCO's visit. Violations of most other health and safety requirements, while common, were usually minor. This category also includes a sub-set of provisions (not shown) specific to factory-provided housing or dormitories.

** **Discrimination**—We believe violations in this area are more widespread than this data suggests. Examples of verified violations included a stated preference for female workers, wrongful termination of pregnant employees, pregnancy testing, inadequate hiring policies and procedures, and higher wages paid to local workers versus foreign workers.

*** **Freedom of Association**—We believe violations in this area are more widespread than this data suggests. Verified violations included failure by management to meet with and recognize lawfully organized unions, retaliation or fear of retaliation against workers who sought to organize and employment applications requiring job candidates to indicate their union affiliation.

2003 FACILITY RATING DATA

COUNTRY	TOTAL NUMBER OF FACTORIES	LEVEL 5 EXCELLENT	LEVEL 4 GOOD	LEVEL 3 FAIR	LEVEL 2 NEEDS IMPROVEMENT	LEVEL 1 IMMEDIATE ATTENTION REQUIRED
El Salvador	9	0	3	2	0	4
Guatemala	7	0	3	0	0	4
Honduras	18	2	7	4	3	2
Lesotho	16	1	1	3	4	7
Cambodia	33	3	17	10	2	1
China	241	11	71	86	48	25

Rating Factories

For long-term improvement of working conditions, we believe our monitoring will be more effective when we can assess how factories perform over time. Compliance isn't just about the issues we identify during a visit, but the types of violations, how quickly they are resolved and how often they are repeated.

In 2002, we developed a tool to help us assess a factory's overall level of compliance through quantifiable metrics. The current rating tool rates factories according to the number, type and pattern of compliance violations during a 12-month period.

Rating factories is harder than it sounds. It requires us to make subjective decisions about the relative importance of different social issues. For example, core issue violations (see Page 12) will negatively impact a factory's rating more significantly than non-core issues. We have been piloting the tool for the past year and a half and the process has been a learning experience. When we evaluated the initial results in mid-2003, we found the ratings did not accurately reflect conditions on the ground. So we revised the metrics, expanded the scale and introduced new weightings according to the severity of the issue.

The chart above shows the 2003 revised ratings for the six countries featured in the case studies that follow. Due to the technical limitations of our system, we are unable to provide data on a global scale at this time. Toward the end of 2004, we will undergo a database conversion that will enable us to capture more detailed information on our monitoring efforts. This new system will allow for more sophisticated analysis of our data and help us to refine our facility rating criteria further. However, as important as these improvements will be to our ongoing reporting efforts, we will be unable to make future comparisons with our 2003 data. Our pilot phase will continue through this system conversion and we will continue to evaluate the tool for accuracy and effectiveness.

THE FIVE LEVELS OF FACTORY RATING

Our current rating tool uses a point scale, which is impacted by the number and type of violations found and the time needed to address them. This scale is grouped into the following levels:

LEVEL 5: Excellent
LEVEL 4: Good
LEVEL 3: Fair
LEVEL 2: Needs Improvement
LEVEL 1: Immediate Attention Required

A factory receives one of five ratings, from Level 5—excellent, where we typically find few or no documented violations, to Level 1—immediate attention required, where we might see many violations, including core and habitual ones. Level 1 factories face losing our business unless management shows immediate improvement in their compliance practices.

Conditions vary from factory to factory. The type of issues (e.g., core, non-core or habitual), the number of times they occur and the time it takes to address them can be present in a variety of combinations. For example, a factory can fall into Level 1 because there are many non-core issues, those issues are habitual and it takes a long time for factory management to address them. On the other hand, another factory at Level 1 may have relatively few non-core issues but a number of core issues identified. In other words, factories with very different compliance pictures can receive the same level rating. ■

Introduction

CHINA

CENTRAL AMERICA

CAMBODIA

LESOTHO

As our factory monitoring and engagement efforts have evolved, we've found that working directly with stakeholders and leveraging our collective efforts produces the best results. In the section that follows, we provide a view into our program: how we put it into action, how key stakeholders view our efforts and where we see our program going.

The case studies included here show the kinds of issues we deal with and how each factory and stakeholder interaction presents us with opportunities. From our experience with independent monitoring in Central America and freedom of association in Lesotho, to the unique challenges offered by countries such as Cambodia and China, we believe that the lessons we've learned help us to continually improve and enhance our program and impact.

We are grateful to our stakeholders who were willing to provide us with their feedback on our program and on this report. This information, taken together with what we have learned from our work in factories around the world, has allowed us to better focus on what we still need to do and to develop our goals for 2004. ■

Stakeholder Feedback

We recently asked some key stakeholders for their views on where our program is and where it should be heading. Each shared insights we can learn from; some themes also emerged.

Participants included: Ineke Zeldenrust, International Coordinator, Clean Clothes Campaign International (CCC); Stephen Coats, Executive Director, United States Labor Education in the Americas Project (US/LEAP); Dan Rees, Director, Ethical Trading Initiative (ETI); Lynda Yanz, Coordinator, Maquila Solidarity Network (MSN); Alice Tepper Marlin, President, Social Accountability International (SAI); Carol Michaels O'Laughlin, Executive Director, Global Alliance for Workers and Communities (GA); Maggie Burns, Trustee, Women Working Worldwide; and Bruce Raynor, President, Union of Needletrades, Industrial and Textile Employees (UNITE).

WHAT IS GAP INC. DOING MOST EFFECTIVELY?

Most stakeholders felt that we do a good job engaging with manufacturers and other stakeholders to address problems as they arise. Our support of training programs for workers and supervisors on workplace issues was viewed as important. They were encouraged by the increased inclusion of multiple stakeholders in the search for more sustainable solutions.

WHAT DOES GAP INC. NEED TO DO BETTER?

Criticisms focused on how we could evolve our program and business practices. We were called upon to drive adoption of a universal code of conduct and institute external verification of our program. Many want us to evaluate production timelines and the prices we pay. By better managing both, they believe we could help decrease overtime needed to fill orders and help manufacturers justify the cost of complying with our code. ■

What Should Companies Do to Improve Working Conditions?

We also asked for their thoughts on what, in general, they thought multinational companies should be focusing on to have a greater impact on factory conditions.

"If significant progress is to be made in the areas of wages and hours, freedom of association and other problematic issues, sourcing strategies need to be rethought, and the drive to reduce costs at any expense must end."
Ineke Zeldenrust, CCC

"Addressing working hours is challenging partly because the issue needs to be tackled on a number of different levels. Persistent low wages put workers in the position of needing to work excessive hours, that in turn can be detrimental to their long term health. More work needs to be done on the concept and application of the Living Wage."
Dan Rees, ETI

"Multinationals should be sending a clearer message to suppliers and local governments that compliance with labor standards is an incentive to sourcing."
Lynda Yanz, MSN

"Companies need to implement sustainable solutions that bring positive benefits to workers and also translate into good business sense for both the brand as well as the manufacturer."
Maggie Burns, Trustee, Women Working Worldwide

"There hasn't been enough emphasis across the industry on empowering workers to exercise their rights. In many cases workers are not even aware of what those rights are."

*Dan Rees, ETI**

"Some recent changes being perceived about Gap Inc. are its willingness to learn from others, its willingness to engage with multi-stakeholder initiatives and its move toward sustainable programming as opposed to a policing model of compliance."

Maggie Burns, Trustee, Women Working Worldwide

"Any country where there is no strong base of civil society groups like NGOs and unions is problematic."

Ineke Zeldenrust, CCC

"**When an issue or problem in a factory arises, it's imperative for companies to involve external stakeholders at an early stage.**"

*Alice Tepper Marlin, SAI**

"We've had our differences with Gap in the past, and we may in the future, but when we started talking with them, we realized we could work together and create positive change for workers."

Bruce Raynor, UNITE

"**While it's encouraging that Gap Inc. has accepted freedom of association and collective bargaining as unassailable rights, they need to improve their enforcement in this area.**"

Stephen Coats, US/LEAP

* We are members of both SAI's Corporate Involvement Program and ETI.

Independent Monitoring

In 1995, the National Labor Committee (NLC), a New York-based workers' rights group, reported alarming abuses at the Mandarin International factory in El Salvador. We dispatched employees to investigate and they returned with firsthand accounts of low pay, excessive overtime and reported union-busting. Most apparel brands and retailers doing business with the manufacturer stopped production and left.

Concerned labor organizations challenged us to take a different approach. They encouraged us to keep production in the factory and work with them to improve conditions. We chose to be part of the solution, instead of just leaving the problem behind.

We collaborated with three NGOs—Business for Social Responsibility (BSR), the Center for Reflection, Education, and Action (CREA), and the Interfaith Center on Corporate Responsibility (ICCR)—to form the Independent Monitoring Working Group (IMWG). The IMWG engaged the Grupo de Monitoreo Independiente de El Salvador (GMIES), a group of representatives from Salvadorean civil society who sought to help workers in the maquila sector. The effort marked the beginning of the first independent monitoring program in El Salvador and in the apparel industry globally.

BENEFITS & CHALLENGES

As we learned the benefits of independent monitoring, we expanded the program to Guatemala in 2000, Honduras and Nicaragua in 2002, and Kenya in 2003.* We have found that independent monitoring can complement our program. Independent monitors are respected members of the local community and enjoy credibility among factory workers. Because they visit fewer factories than our team does, they can focus more deeply on specific facilities, build a greater rapport with workers and discover problems that our team might miss on a given visit. Their independence from both factory managers and us is extremely valuable.

Yet independent monitoring is not without its challenges. We were fortunate in Central America and Kenya to find capable and respected grassroots organizations. Independent monitoring is a relatively new field and many countries simply do not have groups with the necessary skills and resources to take on the task. It takes time and is costly to implement. Unlike external monitoring programs that involve a one-time audit, independent monitoring is an ongoing process of collaboration. Once an issue is identified, our compliance team discusses the findings with the independent monitors and then negotiates a remediation plan with the manufacturer. Our compliance team also continues to maintain their regular monitoring schedules in each factory.

*In Guatemala, independent monitoring is conducted by the Commission for the Verification of Corporate Codes of Conduct (COVERCO). In Honduras, we work with the Independent Monitoring Team of Honduras (EMIH). In Nicaragua, we have engaged Profesionales por la Auditoría Social Empresarial (PASE), which was formed in 2002 as an outgrowth of the Movimiento de Mujeres Trabajadoras y Desempleadas "Maria Elena Cuadra" (MEC). In Kenya, we partner with Africa Now.

LEVEL 5 EXCELLENT	LEVEL 4 GOOD	LEVEL 3 FAIR	LEVEL 2 NEEDS IMPROVEMENT	LEVEL 1 IMMEDIATE ATTENTION REQUIRED
2	13	6	3	10

CENTRAL AMERICA FACILITY RATING DATA

A DIFFERENT APPROACH

In 2002 and 2003, the expansion of our sourcing base to Nicaragua and Kenya—two countries with a long history of labor and social strife—provided a testing ground for a different approach to independent monitoring. For the first time, we incorporated independent monitors into our initial approval process to provide valuable expertise on the ground from the start. During evaluations of new factories, our compliance team focused on health and safety inspections and reviewed documents while the independent monitors interviewed workers. By the end of 2003, our team and the independent monitors found that none of the four facilities evaluated in Nicaragua met our standards, while four of 11 reviewed in Kenya were approved.

We're also working with our independent monitoring colleagues in Central America and other partners to expand worker and management training. We've learned that most cases of non-compliance are signs of bigger challenges. By designing programs that target the root causes of problems and educate and empower workers, we hope to eliminate some of the factors that lead to non-compliance.

Our experience at Mandarin and beyond has taught us that change doesn't happen overnight. But we have learned that real effort does yield real progress. Through continued collaboration with independent monitoring groups, we will strive to continue taking steps forward. ■

Working With Gap Inc. in Central America

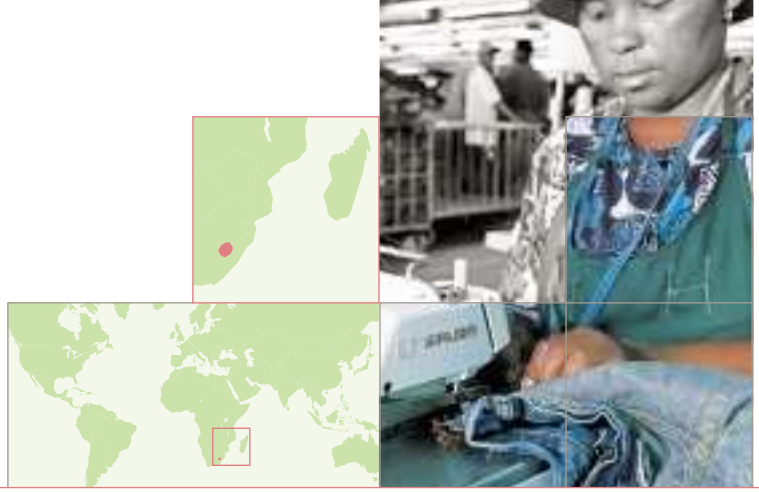
The Regional Initiative for Social Responsibility and Decent Jobs (IRSTD)**

Gap Inc. is one of the few companies doing business in Central America that has adopted social responsibility as part of its business policy, taking seriously the issue of complying with labor rights.

Its suppliers are advised that respect for human rights is part of the company's code of conduct and that producing quality goods in a culture of compliance is a mandatory business requirement; it forms part of the new rules of international commerce. Gap Inc. strengthens these policies by educating their suppliers on how to comply with them. This type of activity is not only improving labor conditions in factories, but also providing an example to the rest of the national and international industrial sector. It also provides an incentive for more businesses to include good practices as a performance indicator of their suppliers.

Certainly there are difficulties to be overcome in order to achieve more improvements and sustainable advances both in physical conditions and in labor relations. Suppliers do not always agree to improve their practices and they can always find other clients that are not as demanding in relation to the human rights of their workers. It is therefore necessary that new incentives motivate suppliers to not only comply with quality and delivery requirements, but also with human rights, especially the labor rights of workers, throughout the supply chain. ■

**The IRSTD is comprised of representatives from the following organizations in Central America: Grupo de Monitoreo Independiente de El Salvador (GMIES); the Commission for the Verification of Corporate Codes of Conduct in Guatemala; the Independent Monitoring Team of Honduras (EMIH); Profesionales por la Auditoría Social Empresarial (PASE) of Nicaragua; the Center for Feminine Studies of the Dominican Republic; and the Association of Labor Promotion Services of Costa Rica.



Freedom of Association

A worker's right to associate freely and not be punished for union activity is an extremely important principle in our Code of Vendor Conduct. We've found that abuses are difficult to discover and prove and even harder to resolve.

Violations of our code's freedom of association requirement are rarely as straightforward as other issues, such as health and safety problems. For example, a worker may allege he was fired because he supported a union; factory management may argue the worker was fired because he consistently was late for work. There may be credible evidence on both sides. Uncovering the truth is challenging, particularly in countries where organized labor is a relatively new concept, and workers, management and governments are learning as they go.

We've found that our ability to discover violations increases when we can conduct in-depth interviews with workers and engage unions and other organizations that have reliable sources in a factory. A valuable learning experience in Lesotho, a small south African country with a relatively young but growing garment industry, helped us evolve how we approach this issue.

DISCOVERING THE PROBLEM; FINDING A SOLUTION

In 2002, MSN, a Canadian-based NGO focused on improving labor standards around the world, contacted us about freedom of association abuses in a Lesotho garment factory.

An incident in that factory later confirmed MSN's concerns that channels of communication between management and the workers had broken down. A worker was injured during an argument with a factory manager. Fortunately, she wasn't seriously harmed, and although the manager claimed the injury was an accident, an investigation into the incident did reveal deep tensions between workers and factory management.

We began investigating and meeting with the Lesotho Clothing and Allied Workers' Union (LECAWU), which represented a majority of the workers at the factory. Union representatives provided examples of how they believed factory management was interfering with workers' efforts to organize legally. UNITE, the U.S.-based apparel union, echoed these concerns.

We initiated talks with factory management and senior executives at the factory's parent company in Taiwan. After months of phone calls and meetings, management agreed to hire new supervisors in the factory. While we were encouraged by its recognition of the importance of hiring management who understood the value of open communication with workers and working productively with unions, we also strongly believed that follow-up was needed to ensure that the change resulted in an improved factory environment. We had many meetings with the

LEVEL 5	LEVEL 4	LEVEL 3	LEVEL 2	LEVEL 1
EXCELLENT	GOOD	FAIR	NEEDS IMPROVEMENT	IMMEDIATE ATTENTION REQUIRED
1	1	3	4	7

LESOTHO FACILITY RATING DATA

new management and provided consultation and reinforcement of our freedom of association expectations. Currently, two unions, including LECAWU, represent workers in this factory.

These efforts led the local branch of the International Textile, Garment and Leather Workers' Federation (ITGLWF) to approach us about further partnership, creating another forum for concerns to be shared and an additional opportunity to work together to address workers' concerns. These discussions have given us greater understanding of freedom of association challenges at the factory level in Sub-Saharan Africa.

OUR ROLE

We strive to protect a worker's right to freedom of association without influencing that choice. We believe in working with garment manufacturers and workers to do all that we can to continually improve conditions and to promote a positive work environment. We also facilitate communication between unions, management and government officials and share concerns we have heard from others or witnessed ourselves. We aim to facilitate workable solutions. Ultimately, government, workers, manufacturers and civil society as a whole must determine how freedom of association is upheld in a country. We're grateful to MSN, UNITE and other stakeholders for engaging us on these issues. Their involvement has helped us better understand the issues and improve our ability to enforce our code requirements. We'll continue learning how to be more effective in this area. ■

Improving Lesotho's Garment Industry

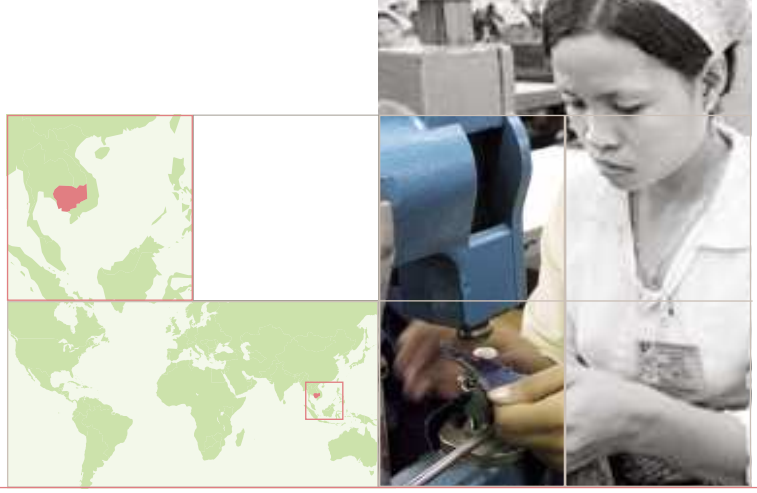
Lena Kopelow

The Global Training Partnership, Fontheim International

With funding so far from two large U.S. retailers, including Gap Inc., the Global Training Partnership's (GTP) pilot project in Lesotho aims to support the local garment industry and government in taking greater ownership over the improvement of factory working conditions and developing solutions. The specific objectives of the project are to provide relevant training and capacity building activities to the Lesotho government, Lesotho Textile Industry Association, and selected garment factories, while also conducting ongoing dialogue with the International Labour Organization and relevant NGOs. The project is scheduled to be implemented over a year's period.

For Lesotho, the GTP project is timely. With the disappearance of mining jobs in South Africa and after over a year of famine, Lesotho's fast-growing garment industry has become critical to the survival of nearly 50,000 workers. Thanks to special preferences under the U.S. African Growth and Opportunities Act, Lesotho's garment industry has seen tremendous growth over the last few years and has become the country's largest employer, exporting over 90 percent of its goods to the United States.

On the ground, GTP is conducting targeted discussions with the government and industry about the growing number of U.S. retailers that take factory working conditions seriously. These brands believe that if Lesotho is to stay globally competitive, good working conditions must become a key part of both industry and government strategies. Through direct dialogue and the provision of key tools and training, GTP aims to help all stakeholders move toward this goal. ■



Cambodia

The use of child labor is one of the most serious violations a manufacturer can commit. Although extremely rare in our approved factories, instances do occur—and in these cases, we take aggressive action. A violation typically results in immediate suspension of production, refusal to accept or pay for merchandise produced and revocation of approval.

Cambodia illustrates how serious labor allegations have actually strengthened our program and expanded our engagement with stakeholders. In 2000, a TV journalist with the British Broadcasting Company (BBC) contacted us with allegations of child labor at a factory in Phnom Penh. We were one of several companies that had production there. The journalist said he had found at least one worker—among about 3,800 at the factory—who was 12 years old, well under Cambodia's legal minimum working age of 15. We immediately contacted our local team and sent additional people to investigate.

At the time, we allowed Cambodian factories to verify a worker's age using a "family book." Because decades of war, genocide and internal strife in Cambodia destroyed many vital documents such as birth certificates, family books were the primary and often the only source of birth dates. The factory's records showed the worker was of legal age, but the journalist said he had traveled to the worker's village and seen a family book showing she was younger. We sent our own team to the village, but could not verify the claim. In October 2000, the BBC aired a report citing the allegation and questioning the effectiveness of monitoring programs such as ours.

The broadcast provoked strong reaction. The worker's age still was unclear and we knew that there was no definitive way to settle the dispute. We were faced with the difficult decision of whether to stay in the factory or leave. As with most factories, this facility had other compliance issues, but none severe enough to warrant revocation. We had been working with the manufacturer to resolve these problems. However, this incident clearly was more serious. We decided to send a strong message that child labor is unacceptable and revoked approval. We also enhanced our age verification requirements at all remaining approved factories in Cambodia. Management must now verify a worker's age in two ways: through the worker's family book and by checking the worker's government-issued country identification or election card.

CREATING PARTNERSHIPS

The garment industry accounts for about a third of Cambodia's gross domestic product and is critical to the nation's economic future. The industry provides jobs for thousands of workers, especially women who may not have many other employment options. For these workers, steady incomes often help educate siblings and stabilize families who are trying to survive on subsistence farming.

Unfortunately, the broadcast prompted some companies to leave the country, and made others hesitant to use Cambodian garment factories. We chose to stay in the country, because it

LEVEL 5 EXCELLENT	LEVEL 4 GOOD	LEVEL 3 FAIR	LEVEL 2 NEEDS IMPROVEMENT	LEVEL 1 IMMEDIATE ATTENTION REQUIRED
3	17	10	2	1

CAMBODIA FACILITY RATING DATA

was important to our business interests and to other manufacturers who were committed to compliance.

We also saw the opportunity to make real progress in labor conditions through collaborative initiatives. The presence of the ILO was an important factor in our decision to remain in Cambodia. Through an ILO-sponsored monitoring program, established as part of the 1999 U.S./Cambodia bilateral trade agreement, Cambodia has one of the world's most monitored garment industries. We support the ILO's monitoring efforts by collaborating with and providing them information regarding our approved manufacturers.

To complement our efforts, we're also supporting the Cambodian Labor Training Coalition (CLTC), composed of the Cambodian Labor Organization, Khemara and the Cambodian Human Rights Task Force. This two-pronged program promotes sustained improvement in the workplace. Factory management is taught about labor relations and modern management models. Workers learn about labor laws, their rights and communication skills. In 2003, the CLTC completed its pilot phase in four factories. We hope to expand the program in 2004. ■

Profile: VannChhai Leng

Senior VCO, Cambodia and Vietnam

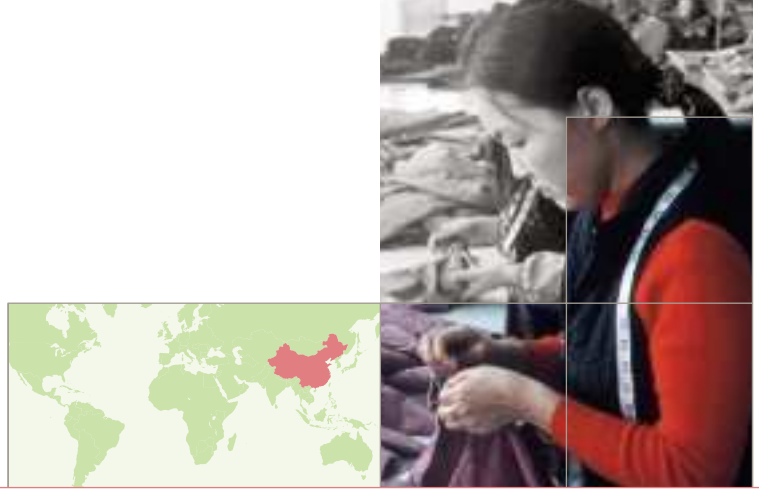
The diversity of our compliance team is core to our program. VannChhai Leng, Senior VCO for Cambodia and Vietnam, has lived through tumultuous periods in Cambodian history. His experiences—from living in a refugee camp in the 1980s to helping organize Cambodia's first labor unions in the 1990s—have given him an ability to understand the difficulties factory workers face.

"I was born in 1962 into a poor farming family and have passed through a difficult life. I didn't have access to formal education or nutritious food. I was eight when the war started. I often had to run for my life during attacks.

"From 1980 to 1992, I stayed in a refugee camp. Then I went home to make a living with nothing but my knowledge from the jungle.

"All life's difficulties are valuable assets. They help me cope with and overcome any situation. It is an asset to be patient, understanding and tolerant. It is important to forgive.

"I am motivated by the positive changes I can bring about, and the chance to make a contribution to my community. When I compare today with life 20 years ago, I work even harder. My experiences help me build friendly relationships with different groups of people, regardless of their background, political affiliation or social status. I try to put myself in their situation. I view it all as a learning process." ■



China

China is the world's largest garment manufacturing market, and most apparel brands and retailers do business there to remain competitive.

Although only one of about 50 countries where Gap Inc. sources merchandise, China is the company's biggest sourcing market. In 2003, the country represented 16 percent of our total merchandise units purchased and 17 percent of total merchandise costs. Because of its size, China's garment industry wields significant global influence, but because of the country's history, political system and culture, it also poses unique and complex compliance challenges. Ensuring that workers' needs and grievances are addressed is especially challenging in a country that doesn't recognize workers' rights to associate freely outside of government-approved organizations.

Our compliance expectations of manufacturers in China are no different than those in any other country. In 2003 China accounted for the highest percentage of factories revoked for compliance violations. Concealment of overtime and unwillingness to share complete and accurate documentation were the main reasons for the high number of revocations. Although these are industrywide issues in China, our VCOs make it clear from their first meeting with potential manufacturers that we will suspend business with any factory found to withhold or fabricate requested documents. A policy is only as good as the willingness to enforce it and we do not hesitate to make good on this threat.

WORKING WITH FACTORIES

Too many manufacturers view compliance as something we impose on them, instead of a smart way of doing business. In 2001, our China team developed an innovative program to encourage manufacturers to assume greater ownership for labor conditions by creating their own compliance programs. We encourage manufacturers to develop their own comprehensive codes of conduct that meet or exceed the standards of their customers. We also advise them on the training of staff to implement the codes and the development of their own internal grievance processes.

These internal factory compliance programs supplement but do not replace our own monitoring. At the end of 2003, approximately 90 out of 241 approved factories in China were participating in this initiative. About a third of these factories have fully embraced the concepts, and we hope to see similar progress in the remaining factories. We believe the program will provide long-term benefits and have begun to apply the concept in other countries.

LEVEL 5 EXCELLENT	LEVEL 4 GOOD	LEVEL 3 FAIR	LEVEL 2 NEEDS IMPROVEMENT	LEVEL 1 IMMEDIATE ATTENTION REQUIRED
11	71	86	48	25

CHINA FACILITY RATING DATA

RUNNING BETTER FACTORIES

Another ongoing challenge we face is the lack of supply chain management skills among some manufacturers. Worldwide, many compliance issues arise from poor management skills and inefficient operating practices. In any workplace, poor supervisory and communication skills often result in worker grievances. Inefficient production lines waste materials and contribute to excessive overtime hours and poor product quality. Since we know that better-run manufacturers and factories have fewer compliance issues, we are exploring ways to help manufacturers strengthen their management skills and improve their overall operations.

In 2003, we initiated a partnership with IMPACTT, a consultancy based in the United Kingdom, and the Hong Kong Productivity Council (HKPC) to help five manufacturers in China improve their supply chains and create better working environments. IMPACTT and HKPC conducted evaluations of each factory and made several key findings. Worker turnover was high, suggesting a variety of problems, including poor internal communication and low pay. Production levels were low because supervisors were not being held accountable for what passed through their sewing lines. Material costs were high due to waste and inefficiency in the production process.

Late in 2003, IMPACTT and HKPC began working with factory managers to develop and implement better operating procedures and management practices. We expect that the manufacturers participating in the program will benefit from and embrace these practices as a better way of doing business. If the initial pilot is successful, we hope to expand the program in 2004. We look forward to reporting on our progress. ■

Helping Workers Understand Their Rights: Mingyu Chen

Many Chinese garment workers travel a long way from home to work in factories. They face tremendous difficulties—discrimination in the cities, mistreatment by recruitment agents and factory supervisors and a lack of knowledge about their rights under Chinese provincial and local law.

In 2002, we approached Mr. Mingyu Chen about speaking to garment workers regarding their rights. Mr. Chen was 17 when he left his home village to work in China's industrial zone, and he understands firsthand the challenges migrant workers face. In 2000, after four years of studying law at night, he realized workers needed help. He started a workers' telephone hotline. In the past three years, Mr. Chen has provided free legal consultation to more than 12,000 callers.

Mr. Chen was hesitant about working with a multinational company. However, after consideration, he agreed to conduct voluntary lunchtime training sessions at several of our approved manufacturers. In each session, Mr. Chen reviews Chinese labor law, the rights of workers and management's responsibilities. He advises workers how to seek recourse if their rights are violated. He also hands out his card and invites them to call if they need help.

Mr. Chen provides workers not only with knowledge, but also the possibility of solutions. To date he has visited about 20 percent of our approved manufacturers in China. We hope he will eventually reach all of them. ■

Since late 2002, Gap Inc. has been working with a group of stakeholders to explore opportunities for greater transparency and increased sustainability of our work. Five organizations comprise the Public Reporting Working Group: Domini Social Investments, the Calvert Group, the As You Sow Foundation, the Center for Reflection, Education and Action (CREA) and the Interfaith Center on Corporate Responsibility (ICCR).

Increasing Transparency

Public Reporting Working Group Statement

As socially responsible investors, we engage in long-term dialogue with corporations, seeking to encourage the development of compliance systems that will consistently work to improve the conditions under which workers earn their living throughout the global supply chain. This report is the result of one such ongoing dialogue.

When we began discussions with Gap Inc., we were seeking greater public transparency. We wanted to understand what Gap Inc. is doing and how it responds to specific situations. We wanted to be able to pick up a report and review Gap Inc.'s performance over time, and relative to its peers. Today, there is no generally accepted reporting format for supply chain compliance. Eventually, we hope that this dialogue will produce a model format that other companies can adapt, and improve upon. Gap Inc. has engaged in this process with creativity and enthusiasm, and it has been our pleasure to participate.

This report is a summary of Gap Inc.'s compliance efforts during 2003. As such, it helps us to see what has been done, what could have been done better, and what needs to be changed for the future. What is obvious throughout is that compliance is intended to benefit workers. In our view, corporate social compliance systems should exist to bring working conditions in line with internationally accepted human rights standards. These systems are critically important to helping workers protect their rights. We commend Gap Inc. for recognizing that its code of conduct sits within this broader context of international human rights norms. It is an important recognition of public accountability.

This report contains a great deal of information that many companies have not provided publicly, and includes valuable insights from a company that we believe is sincerely struggling with these complex issues. Importantly, it illustrates the need for partners from among the broad spectrum of NGOs including groups from the human rights, labor and religious sectors. It reminds us over and over that compliance is a process, and it is not easy.

We expect that in the future, the company will provide the public with factory specific data to permit stakeholders to better understand the complexities of compliance and to measure Gap Inc.'s performance over time. In essence, it should provide the substance of public accountability expected of any leading company.

Gap Inc. has been recognized for its leadership in independent monitoring as a component of ongoing compliance. This report is a strong first step toward establishing Gap Inc. as a leader in public reporting as well. ■

Adam Kanzer, Esq., Domini Social Investments LLC
Alya Z. Kayal, Esq., Calvert Group Ltd.
Conrad MacKerron, As You Sow Foundation
Ruth Rosenbaum, TC, Ph.D., CREA: Center for Reflection, Education and Action, Inc.
David M. Schilling, Interfaith Center on Corporate Responsibility

Looking Forward

Not long ago, a code of conduct was a new concept for global apparel brands. Now, it is a norm in our industry. While the proliferation of codes has led to new goals—such as efforts to develop a universal code and more consistent enforcement—it also demonstrates progress. Experience has opened us up to a broader perspective and deeper understanding of labor issues. We have learned repeatedly that working together is more effective than working alone. Our industry is too fragmented and the issues are too broad, too complex and too fluid for one company to have substantial or sustained impact.

Leadership in this area means something different today than it did a decade ago when our Global Compliance department was formed. While we have developed a strong internal monitoring program, we recognize that monitoring alone is not enough. Broad-based ownership of and accountability for labor standards is most likely to grow from innovation, engagement and collaboration with both internal and external partners.

OUR MONITORING PROGRAM

Factory monitoring will remain an important part of our program. It is critical for us to know what is happening in the factories that produce our clothes and to enforce our code. To help us better assess the strengths and weaknesses of our program, SAI will conduct a review of our compliance systems and processes in 2004. A summary of this evaluation will be made publicly available.

OUR SUPPLY CHAIN

We recognize that opportunities remain to improve labor standards by achieving alignment within our own supply chain. In 2004, we will continue our work to identify and address supply chain practices, such as frequent changes to or rushing of orders, that may impact working conditions in factories.

2004 Key Goals

- Participate in an SAI pilot compliance program evaluation.
- Support multi-stakeholder efforts to develop universal code of conduct.
- Identify supply chain practices that may impact factory working conditions.
- Broaden worldwide stakeholder engagement and initiatives.

OUR EXTERNAL ENGAGEMENT

We will continue to expand our global external engagement efforts in 2004. The success of worker training programs in China and Cambodia has encouraged us to pilot similar programs in Central America. Our involvement with organizations such as SAI, GA and ETI is opening up a dialogue with other global brands, and encouraging us to pursue more collaborative projects. This will allow us to leverage the experience of others to develop and achieve common objectives to improve working conditions across the industry. We hope that these multi-stakeholder efforts will help foster greater industry responsibility for the creation and enforcement of labor standards.

This report is a first step toward our goal to provide greater transparency into our compliance program. We will continue to share more about our efforts through our Web site and other external communications. We look forward to your feedback and to reporting further on our progress in 2005. ■

Currently, our Board has 13 directors, nine of whom are independent of the company and its management.

Corporate Compliance and Governance

BROADER COMMITMENTS

Just as our Code of Vendor Conduct sets forth ethical operating standards for garment manufacturers, our internal ethics code—the Code of Business Conduct—governs our own business practices. These codes help us ensure that social responsibility—whether reflected in how we run our business and manage our environmental impacts or how we support our employees and the communities where they live and work—is ingrained into how we do business.

CORPORATE COMPLIANCE & GOVERNANCE

We believe that good corporate compliance and governance means going beyond what we have to do. It means being a leader, especially in business ethics, and ensuring that we communicate frankly with our shareholders, customers and employees. We are committed to continually evolving our corporate compliance and governance programs in line with legal and regulatory requirements, corporate ethics best practices and our own high standards.

BOARD INDEPENDENCE

Currently, our Board has 13 directors, nine of whom are independent of the company and its management. At every Board meeting, time is set aside for the independent directors to meet without the presence of management. In 2003, the Board appointed a Lead Independent Director who chairs these meetings. Only independent directors may serve on the Board's three committees—Governance, Nominating and Social Responsibility; Audit and Finance; and Compensation and Management Development.

BOARD ENGAGEMENT

Our directors make a significant time commitment to ensure the Board is actively engaged. New members are expected to participate in a formal onboarding program. In addition, the Board has adopted a continuing education program for existing directors. The full Board meets every other month and Board members often work with management outside of formal meetings. Board members participate in a two-day annual strategy meeting as well.

BOARD DEVELOPMENT & EFFECTIVENESS

The Governance, Nominating and Social Responsibility committee annually reviews and assesses the composition and overall performance of the Board, its committees and each individual director. As part of this process, each Board member must participate in an extensive performance evaluation process, including individual peer assessment, in order to be nominated for re-election.

CODE OF BUSINESS CONDUCT

All Gap Inc. employees and directors must adhere to our Code of Business Conduct, which is designed to avoid conflicts of interest, achieve compliance with laws and protect our company assets. Reflecting the global reach of our company and diversity of our employees, the Code of Business Conduct is published in 10 languages. We regularly remind employees of their obligation to act responsibly and with integrity when conducting our business by reinforcing the code through employee communications, including workplace posters, distribution of the card shown at the top of Page 31, regular articles on our internal Web site and employee training sessions.

Gap Inc.
CODE OF BUSINESS CONDUCT
Code Hotline

Callers from the U.S., Canada and Puerto Rico call
1-866-GAP-CODE (toll free)

International callers **1-770-582-5221**
(operator assisted free call)

Doing the Right Thing

TRANSPARENCY
We make sure that key corporate compliance and governance information and documents are accessible to shareholders and other stakeholders. Our Corporate Governance Guidelines, Board committee charters, Code of Business Conduct and other information about our company's practices are all available at gapinc.com.

COMMUNICATION
Our shareholders, customers, employees and the public can communicate directly with the Board regarding any governance matter by emailing board@gap.com. Our Chairman and our Lead Independent Director, as well as our Corporate Compliance and Governance team, reviews every email received.

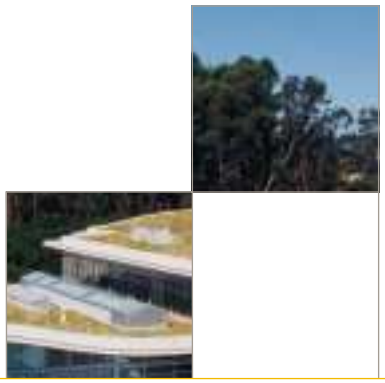
This Board email is yet another way—in addition to our Code of Business Conduct hotline—that anyone can contact the company regarding our business practices. Our Code of Business Conduct hotline allows anyone to confidentially and, if desired, anonymously report concerns regarding our business practices by calling (866) Gap-Code in the United States, Canada and Puerto Rico (toll-free) or (770) 582-5221 elsewhere (operator-assisted free call). Code of Business Conduct concerns may also be sent directly to our Corporate Compliance and Governance team by emailing them at corporate_compliance@gap.com.

Code Violations to Report

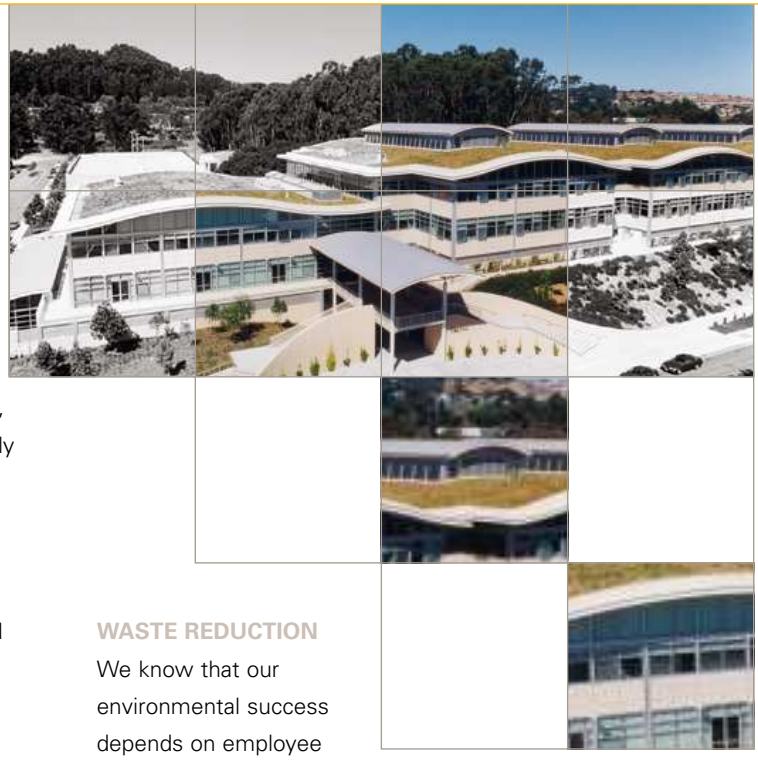
- Accommodations for disability
- Accounting or auditing concerns
- Conflict of interest
- Discrimination or harassment
- Fraud or theft
- Health and safety
- Inaccurate recordkeeping
- Insider trading
- Workplace violence
- Any other suspected code violation

CORPORATE COMPLIANCE & GOVERNANCE DEPARTMENT
Under the guidance of Executive Vice President, Chief Administrative and Compliance Officer Anne Gust, the company's Corporate Compliance and Governance department leads the company's efforts to promote and enforce compliance with our Code of Business Conduct, the foundation of our corporate compliance program. The Corporate Compliance and Governance team monitors and audits code compliance, raises code awareness through employee communication and education and investigates and responds to all suspected code violations.

A combination of written guidelines, formal processes and management oversight helps us ensure that strong corporate compliance and governance isn't just words on paper, but a way of doing business at Gap Inc. ■



Environment



We understand that the operation of our stores, distribution centers and offices and how we use natural resources—whether it is for construction, office supplies or marketing materials—affects the environment. Our goal is to balance our environmental impacts with our business needs.

CONSERVING ENERGY

We are constantly looking for ways to reduce our energy use. One way we have succeeded is by improving our store design, building standards and operations. Stores built today are roughly 25 percent more energy efficient per square foot than those opened in 2000, and almost 29 percent more efficient than those built in 1990.

Energy use in about 40 percent of our U.S. stores is monitored through a computerized energy management system (EMS). EMS enables us to monitor system performance and identify opportunities to further reduce our energy consumption.

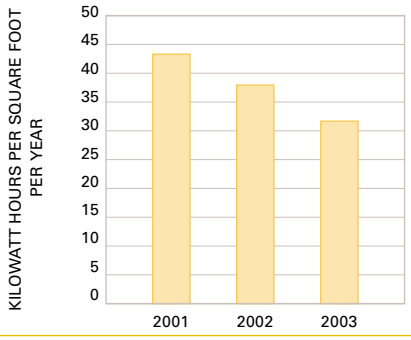
By taking simple steps at our distribution centers, such as resetting thermostats, installing energy-efficient light fixtures and automatic controls for conveyor systems, we've decreased energy consumption by approximately 15 percent. These and other improvements in our logistics division have resulted in average annual savings of nearly $1.6 million since 2001.

We've received recognition for our environmentally sustainable buildings, such as our corporate offices at 901 Cherry Avenue in San Bruno, California (pictured above), and our new headquarters building in San Francisco (see Page 33). The use of innovative features such as a grass roof and fly ash in these projects has inspired others to incorporate them into their buildings.

WASTE REDUCTION

We know that our environmental success depends on employee participation. All employees are asked to reduce waste, recycle and purchase products that contain post-consumer recycled material. In 2003, we recycled approximately 20,000 tons of paper and cardboard. Many of the cardboard boxes we use have a minimum post-consumer or recycled content of 20 percent, and some with content as high as 30 percent.

The standard paper used in our corporate offices has 30 percent post-consumer content and all copy machines have been programmed to default to making two-sided copies. In 2003, we initiated a composting program at our employee cafes in our San Francisco Bay Area headquarters offices. This allows us to divert approximately 15,600 pounds of waste from landfills each month that is turned into nutrient-rich topsoil.



AVERAGE ENERGY CONSUMPTION IN GAP INC. U.S. STORES

COMPLYING WITH ENVIRONMENTAL REGULATIONS

We want to make it easy for our employees to meet the most basic of our ethical standards—complying with the law. Gap Inc.'s environmental compliance program is comprised of procedures, policies, guidelines and trainings to assist employees throughout the company to comply with local, state and federal environmental regulations.

MOVING FORWARD

The following initiatives are examples of ways we hope to keep moving our environmental practices in the right direction:

Climate Leaders—In 2003, we joined the U.S. Environmental Protection Agency's Climate Leaders program. This voluntary partnership between industry and government encourages companies to reduce their greenhouse gas emissions.

Environmental Metrics—In 2004, we plan to implement a companywide tracking system to better capture and measure what we currently do and to set priorities for our future environmental efforts, as well as increase transparency.

Water in Manufacturing Facilities—We have been instrumental in working with Business for Social Responsibility to bring together a group of apparel companies to share best practices and collaborate on an industrywide standard to improve garment manufacturers' wastewater treatment. While we have tried to implement our own programs in the past, we hope this collaborative approach will result in greater, more sustainable improvements. ■

Environmentally Sustainable Buildings

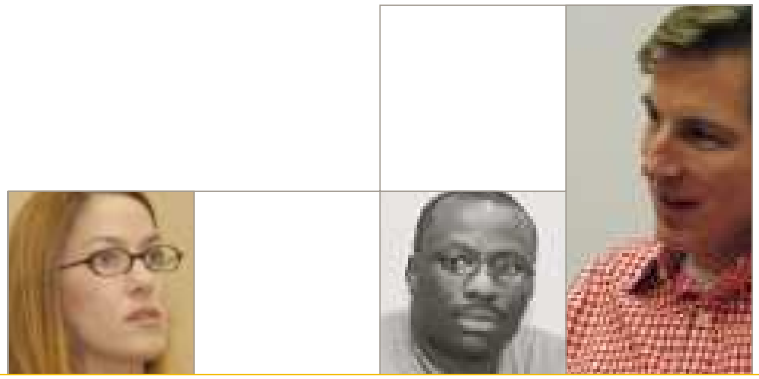
Since its completion in 1997, our 901 Cherry Avenue building—part of our San Bruno, California, headquarters campus—has been heralded for providing a quality work environment while minimizing its impact on our natural resources and the environment.

One of the building's most striking features is the roof—it's covered in native grasses. An excellent insulator, this unique covering provides increased energy savings year-round. It also restores natural habitat and reduces runoff during the rainy season.

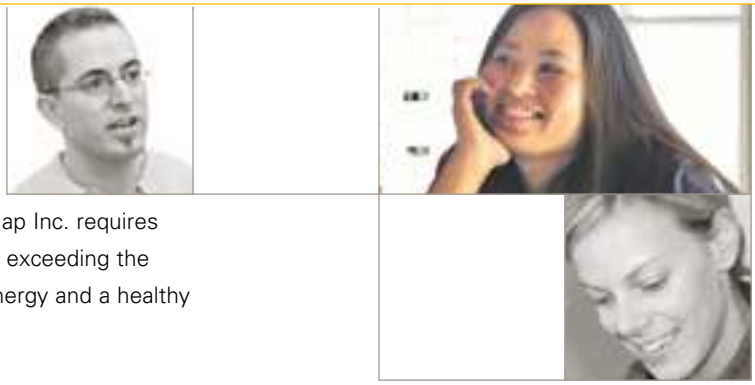
Unlike most office buildings, the exterior windows actually open. In addition, an under-floor ventilation system stores cold night air and uses it to cool the building throughout the day. The extensive use of windows provides natural light. When artificial lighting is used, computer-activated lamps gradually fill in for the fading daylight. Occupancy sensors turn lights off when personal offices and conference rooms are vacant.

Almost all interior wood and wood veneer used for floors, doors and wall paneling was harvested from certified, well-managed forests. Low-toxic paints, carpets and tile adhesives, as well as formaldehyde-free particleboard are used throughout.

Our newest building in San Francisco promoted ecological construction in another way. Fly ash, a waste by-product from coal-burning power plants, was used in the concrete for the foundation. Not only did this project divert 1,800 tons of fly ash from landfills, it also eliminated approximately 2,000 tons of carbon dioxide emissions that would have been generated during cement production. That's the equivalent of roughly 350 people not driving their cars for an entire year. ■



Our Employees



Gap Inc. is made up of smart, diverse, fun, talented individuals working around the world in areas from design to distribution to marketing to merchandising. Working at Gap Inc. requires a passion for our products, a commitment to exceeding the expectations of our customers, boundless energy and a healthy dose of creativity.

With more than 150,000 employees around the globe, Gap Inc. has a responsibility to maintain a workplace in which they can thrive. Beginning on the first day of employment, we inspire our individuals and teams to reach their full potential through a variety of development programs. Training curriculums and learning environments range from classroom sessions to in-store experience; from on-the-job coaching with a supervisor to online resource guides and tools. Ensuring an ethical, inclusive work environment and comprehensive, competitive benefits programs for our employees worldwide is equally key to our efforts.

AN ETHICAL & INCLUSIVE WORKPLACE

Having a diverse workforce and clearly defined workplace policies is not just a well-intentioned goal—it's essential to how Gap Inc. does business.

In fact, Gap, Inc. ranked fourth highest among California-based companies on the Fortune 1000 list for the percentage of women on its Board of Directors. Four directors of our 13-member Board are women, more than double the state and national averages. Currently, five of the 12 top Gap Inc. executives are women.

At Gap Inc., we believe diversity reflects more than physical traits; it involves how individual differences—in experience, culture, opinion, style and viewpoint—influence the way we work with each other and serve our customers. We are an equal opportunity employer and strictly enforce our "Zero Means Zero" policy regarding harassment and discrimination. To expand these efforts, we created a global diversity council that is developing strategies and recruiting a Vice President of Diversity, a new position we hope to fill in 2004.

Our global Code of Business Conduct further demonstrates our commitment to providing a responsible and ethical work environment for all our employees. It contains guidelines on proper workplace behavior and how to raise questions or concerns. Our hotline allows employees—or any member of the public—to anonymously report code violations at (866) Gap-Code in the United States, Canada and Puerto Rico (toll-free) or (770) 582-5221 elsewhere (operator-assisted free call).

HEALTH, WELLNESS & LIFESTYLE

Gap Inc. offers a range of programs for our employees. Benefits range from a generous merchandise discount to a gift-matching program for both charitable donations and volunteer time. Full-time employees also have access to medical, dental, vision, life and disability insurance and our Employee Assistance Program, a confidential service that provides resources for employees and their families coping with personal issues. In addition to a generous Paid Time Off (PTO) plan, employees can donate their earned time off to co-workers in need through the PTO Donation Fund. We are continuing to expand our free employee wellness programs, including a new health information Web site, 24-hour medical hotline support and a healthy pregnancy program.

Gap Inc. supports new parents in a variety of ways. Parental leave is available for both the birth and adoption of a child, and flexible phase-in and phase-out scheduling provides an easier transition both out of and back into a regular work schedule.

In the United States, most benefits are available to full-time employees on their first day and are extended to their eligible dependents, including children, spouses and same-sex life partners. In other countries, similar benefits are offered depending on the benefit plan and location. In 2003, we spent more than $500 million on benefits worldwide.

SUPPORTING FINANCIAL HEALTH

The financial well-being of our employees is very important. In addition to providing competitive compensation programs, we offer a 401(k) plan to employees with one year of employment that features dollar-for-dollar company matching contributions up to four percent of pay, with 100 percent immediate vesting. Employees can participate in our Employee Stock Purchase Plan (ESPP) and purchase Gap Inc. stock at a discount that's at least 15% below market rates. Last November, Gap Inc.'s ESPP purchase represented a $5 million savings for employees. Employees also can access free financial planning services to help them get the most out of these programs and achieve their financial goals.

Gap Inc. offers tuition reimbursement to qualified employees so they can enroll in classes to enhance their job knowledge and skills. The company spends about $1.4 million per year on this tuition reimbursement program.

We know that our business success depends on Gap Inc. giving our employees meaningful work and great careers. That's why making our company a great place to work and a true community for our employees will always be a top priority. ■

Community Involvement

For nearly three decades, Gap Inc.'s charitable arm, Gap Foundation, has spearheaded the company's community involvement efforts through grants, in-kind donations, community outreach and employee volunteer programs.

GIVING MONEY

During the past five years (1999-2003), Gap Foundation distributed approximately $60 million in cash grants worldwide, representing approximately one percent of net earnings before taxes for the period. Through the Gap Foundation, the company also makes substantial product donations each year. For example, in 2003, more than $12 million in product donations were made to non-profit organizations to help people in need. Recipient organizations range in size from national groups, such as Boys & Girls Clubs of America (B&GCA), to local projects, such as the rebuilding of the Zabalaza Junior Primary School in South Africa.

In 2002, B&GCA launched its first ever Web-based program. CareerLaunch™—a career exploration program fully funded by Gap Foundation—is designed to help teens make sound educational decisions, learn about career opportunities and prepare for the workforce. CareerLaunch™ is available to more than 3,300 Boys & Girls Clubs nationwide (see Page 38).

A snapshot of other organizations funded by Gap Foundation:

• **Harlem Children's Zone** (New York)—This pioneering, non-profit, community-based organization works to enhance the quality of life for children and families in some of New York City's most devastated neighborhoods. Their 15 centers serve more than 12,600 children and adults.

• **Sojourn to the Past** (San Francisco Bay Area)—An educational program through which high school students and educators visit the most dramatic sites of the civil rights movement in the United States. Participants learn the real lessons of the movement—tolerance, justice, compassion, hope and non-violence.

• **Sargent Cancer Care for Children** (UK)—This national charity funds a network of skilled social workers in all major cancer centers in the United Kingdom, offering counseling, financial help and practical care to critically-ill children and their families.

• **CARE** (Cambodia)—A health program that targets the needs of garment workers and their families, this program improves access to clinical services for workers and promotes education, awareness and prevention of HIV/AIDS and other sexually transmitted diseases for workers and factory clinic staff.

EMPLOYEE GIVING

Gap Foundation matches, dollar-for-dollar, the charitable donations of individual employees to qualifying organizations—up to certain limits.

The Gap Foundation supports organizations focused on children, youth and families. *Immediately left,* Marka Hansen, Banana Republic President, and friends at Halloween pumpkin patch event. *Opposite page, lower right,* former President Jimmy Carter in front of Gap Inc. funded—and employee-built—Habitat for Humanity house.

GIVING TIME

In 2003, Gap Inc. employees volunteered nearly 22,000 hours of company-paid time through Gap Foundation volunteer programs. The Foundation's "Take Five" program allows headquarters employees five hours of time off per month to volunteer during the workday.

The "Money for Time" program encourages employee volunteerism by providing cash grants to organizations where employees volunteer. For every 15 hours an employee volunteers at a qualified organization, the Foundation grants that organization $150.

Gap Inc. also recognizes dedicated employee volunteers through the "Community Corps" program. Employees apply for the opportunity to build homes in partnership with Habitat for Humanity International. Gap Foundation provides 100% of the funding needed to build these homes. The program began in 2000 and to date we've funded and built more than 25 homes in Alaska, Alabama, Arizona, Georgia, Mississippi, Tennessee and in Honduras, Mexico, Guatemala and El Salvador. ■

Community Corps

Community Corps was created for employees like Jennifer, a Banana Republic store manager in the Boston area.

A longtime community volunteer, Jennifer has participated in the Walk for Hunger, the Boston to New York AIDS ride, and has volunteered at the New England Aquarium for 10 years.

She was one of 30 Gap Inc. employees selected for the Community Corps project in Honduras in September of 2002.

"I'll never forget the first day. The mother, Ina, came by the house and when she saw us, she came and hugged us and kept thanking us," says Jennifer. "It made me realize what a huge impact we were having on this family."

The trip also taught her a lot about the company and her co-workers.

"It was eye-opening to find out about what Gap Foundation does and really inspiring to learn how other people across the company were involved in their communities."

Since her Community Corps trip, Jennifer has returned to Honduras to work on Habitat projects several times. In February 2003 she helped lead a team there and was able to share her past experiences.

"In one section of the training they talked about Gap Inc.'s Community Corps. I was able to tell the group that that was how I got involved with Habitat," she says. "Everyone was so impressed that my employer did something like that. It really made me proud to work for this company." ■

"Gap Foundation isn't just about giving money; it's about giving hope—often to those who feel they have none."
Dotti Hatcher, Vice President, Gap Foundation

Community Involvement

Helping Teens Find Their Paths

Today's teens are faced with a tremendous number of educational and career options. Many just don't know where to start in deciding where to go to school or how to look for that first full-time job. Boys & Girls Clubs of America's CareerLaunch™ program—funded by a $7.5 million Gap Foundation grant over seven years—aims to help students take some of the guesswork out of their educational and career decisions.

The program incorporates a strong mentoring element with practical resources teens can use. Participants research school and career options on the CareerLaunch™ Web site. There they can assess their interests and access job profiles that parallel them. They also can garner information on approximately 9,000 colleges and technical schools, determine their eligibility requirements and can even apply for financial aid. There's also an easy-to-use career exploration guide that offers a range of career planning and job skills exercises that Club staff or volunteers can use with teens.

"CareerLaunch is truly a 'generation-changing' program," says Roxanne Spillett, President of Boys & Girls Clubs of America. "It not only teaches Boys & Girls Club teen members how to become more employable today, it also equips them with the know-how to make one of the most important decisions of their lives—their choice of career."

The program's real-world applicability is a key component. Each participant receives a resource guide with practical interviewing and job tips. Everything from how to fill out a job application and dress for an interview, to how to write a resume and cover letter is included.

Through CareerLaunch™, Gap Foundation is helping Boys & Girls Clubs enable teens to successfully transition into the challenging job market. We hope that it allows them to imagine what their future could be while helping them take concrete steps to get there.

"CareerLaunch is truly a 'generation-changing' program," says Roxanne Spillett, President of Boys & Girls Clubs of America.

FEEDBACK

Gap Inc.

We want to know what you think about this report, so please let us know how we did. Your feedback is essential in helping us expand and improve our social responsibility efforts. Thank you.

1. What was your opinion of Gap Inc.'s social responsibility efforts **before** reading this report?

EXTREMELY UNFAVORABLE				*EXTREMELY FAVORABLE*
1	2	3	4	5

2. What is you opinion of Gap Inc.'s social responsibility efforts **after** reading this report?

EXTREMELY UNFAVORABLE				*EXTREMELY FAVORABLE*
1	2	3	4	5

3. On a scale of 1 to 5, with five being excellent, rate the following components of the report:

Overall Report	1	2	3	4	5
Overall Labor Standards Information	1	2	3	4	5
Labor Standards Data	1	2	3	4	5
Labor Standards Case Studies	1	2	3	4	5
Other Areas of Social Resonsibility	1	2	3	4	5

4. I am a/n (optional):

- ☐ Customer
- ☐ Gap Inc. Employee
- ☐ Representative of a non-governmental organization
- ☐ Shareholder
- ☐ Student
- ☐ Other _____ *PLEASE SPECIFY*

If you have other thoughts on our report or on how we can better communicate about our social responsibility efforts, please email us at **social_responsibility@gap.com.**

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Glossary

Business for Social Responsibility (BSR)—A global organization that helps member companies achieve success in ways that respect ethical values, people, communities and the environment. For more information, visit them at www.bsr.org.

Cambodian Labor Training Coalition (CLTC)—Composed of the Cambodian Labor Organization, Khemara and the Cambodian Human Rights Task Force, a two-pronged training program that promotes sustained improvement in the workplace.

Child labor—As defined in the Gap Inc. Code of Vendor Conduct, the employment of workers who do not meet the applicable minimum legal age requirement or are not at least 14 years of age, whichever is greater.

Code of Vendor Conduct—Basic requirements set forth by Gap Inc. that all manufacturers and factories must be able to meet in order to do business with the company. The code provides the foundation for Gap Inc.'s ongoing evaluation of a manufacturer's employment practices and environmental compliance.

Code of Business Conduct—Gap Inc.'s internal ethics code that governs business practices and is designed to help the company and its employees avoid conflicts of interest, achieve compliance with laws and protect company assets, including employees and properties.

Corporate Governance and Compliance—The Gap Inc. department responsible for enforcing the company's Code of Business Conduct and ensuring that the company's practices and policies are in keeping with legal and widely accepted ethical standards.

Ethical Trading Initiative (ETI)—An alliance of companies, NGOs and trade union organizations committed to working together to identify and promote ethical trade. For more information, visit them at www.ethicaltrade.org.

Forced labor—As defined in the Gap Inc. Code of Vendor Conduct, prison, indentured, debt bondage or involuntary labor of any kind.

Foreign contract workers—Workers who sign an employment contract to work at a factory outside their home country.

Freedom of association—As defined in the Gap Inc. Code of Vendor Conduct, the right of workers to lawfully join associations of their own choosing, peacefully associate, organize or bargain collectively.

Garment manufacturers—Third-party manufacturers with whom Gap Inc. contracts to make its apparel. Sometimes, a garment manufacturer has only its own facility. Other times, it may own more than one factory and/or subcontract with others.

Global Alliance (GA)—A partnership of private, public and NGOs established to improve the workplace experience and future prospects of workers involved in global production and service supply chains in developing countries. For more information, visit them at www.theglobalalliance.org.

Global Compliance—The Gap Inc. department responsible for enforcing the company's Code of Vendor Conduct in the manufacturing facilities that produce its apparel and for stakeholder engagement in the area of labor standards and working conditions.

Global Reporting Initiative (GRI)—A multi-stakeholder process and independent institution whose mission is to develop and disseminate globally applicable sustainability reporting guidelines. For more information, visit them at www.globalreporting.org.

Hong Kong Productivity Council (HKPC)—A multidisciplinary organization established by statute in 1967 to promote increased productivity and the use of more efficient methods throughout Hong Kong's business sectors. For more information, visit them at www.hkpc.org.

IMPACTT—A UK-based consultancy group that works with companies, organizations and individuals to develop business practices which extend the number of people who benefit from international trade and investment. For more information, visit them at www.impacttlimited.com.

Independent monitoring—Ongoing monitoring of working conditions conducted by local non-profit, civil society organizations at the request of companies or international organizations. Independent monitoring groups usually report their findings publicly.

Independent Monitoring Working Group (IMWG)—A collaboration between Gap Inc., Business for Social Responsibility, the Center for Reflection, Education, and Action, and the Interfaith Center on Corporate Responsibility, which resulted in the first independent monitoring program in El Salvador and in the apparel industry globally.

International Labour Organization (ILO)—The United Nations (UN) specialized agency that seeks the promotion of social justice and internationally recognized labor rights.

Maquila Solidarity Network (MSN)—A Canadian-based NGO focused on improving labor standards around the world. For more information, visit them at www.maquilasolidarity.org.

Multilateral organizations—International organizations consisting of multiple nations and/or other significant parties.

Non-governmental organizations (NGOs)—National, international and community-based groups that raise awareness about social, environmental, community and human rights issues.

Public Reporting Working Group—A group of stakeholders Gap Inc. has been working with since late 2002 to explore opportunities for greater transparency and increased sustainability of our work. This working group is comprised of Domini Social Investments (www.domini.com), the Calvert Group (www.calvertgroup.com), the As You Sow Foundation (www.asyousow.org), the Center for Reflection, Education and Action (www.crea-inc.org), and the Interfaith Center on Corporate Responsibility (www.iccr.org).

Quality Assurance—A part of the Gap Inc. sourcing organization, the department that works with manufacturers to ensure products meet Gap Inc. expectations in terms of construction, measurements and safety requirements.

Social Accountability International (SAI)—A US-based, non-profit organization dedicated to the development, implementation and oversight of voluntary verifiable social accountability standards. For more information, visit them at www.sa-intl.org.

Sourcing—The process by which Gap Inc. selects and places orders with manufacturers around the world to produce the merchandise sold in its stores.

Stakeholders—Individuals and groups including NGOs, unions, governments, suppliers, shareholders and employees who have a vested interest in the way companies conduct their business.

Universal code of conduct—A unified code of vendor conduct used across an industry. This is a goal of many multi-stakeholder groups.

Vendor Compliance Officer (VCO)—A member of Gap Inc.'s Global Compliance department who monitors working conditions of manufacturers producing goods for the company.

Gap Inc. is a leading international specialty retailer offering clothing, accessories and personal care products for men, women, children and babies under the Gap, Banana Republic and Old Navy brand names. Gap Inc. operates about 3,000 stores in the United States, the United Kingdom, Canada, France, Japan and Germany.* In the United States, customers also may shop the company's online stores at gap.com, BananaRepublic.com and oldnavy.com.

Gap Inc. Overview

Fiscal 2003 Highlights

Sales: $15.9 billion

Earnings: $1.0 billion, or $1.09 per share on a diluted basis

Employees: more than 150,000 at fiscal year-end

Social Responsibility Highlights

Social Investment Indexes: Gap Inc. is listed** on: Calvert Social Index, Domini 400 Social℠ Index, Dow Jones Sustainability Index, FTSE4Good US 100 and FTSE4Good Global Indexes

Ethical Sourcing/Global Compliance

- Merchandise produced by third-party garment manufacturers using approximately 3,000 garment factories in about 50 countries, including the United States
- Garment manufacturers and factories required to undergo comprehensive Gap Inc. Code of Vendor Conduct evaluation before being approved for production
- More than 90 full-time Gap Inc. employees worldwide focused exclusively on monitoring and improving factory conditions, labor practices and compliance with company standards

Employee Volunteerism and Community Support

- Gap Inc. employees volunteered 22,000 hours in 2003 through company programs
- $60 million donated to non-profit organizations worldwide during the past five years, in addition to $12 million in in-kind contributions in 2003 through the Gap Foundation

Environment

- Stores built in 2003 are roughly 25% more energy efficient per square foot than those opened in 2000, and almost 29% more efficient than those built in 1990
- Gap Inc. recycled 20,000 tons of cardboard and paper in 2003
- Member of U.S. Environmental Protection Agency's Climate Leaders Program

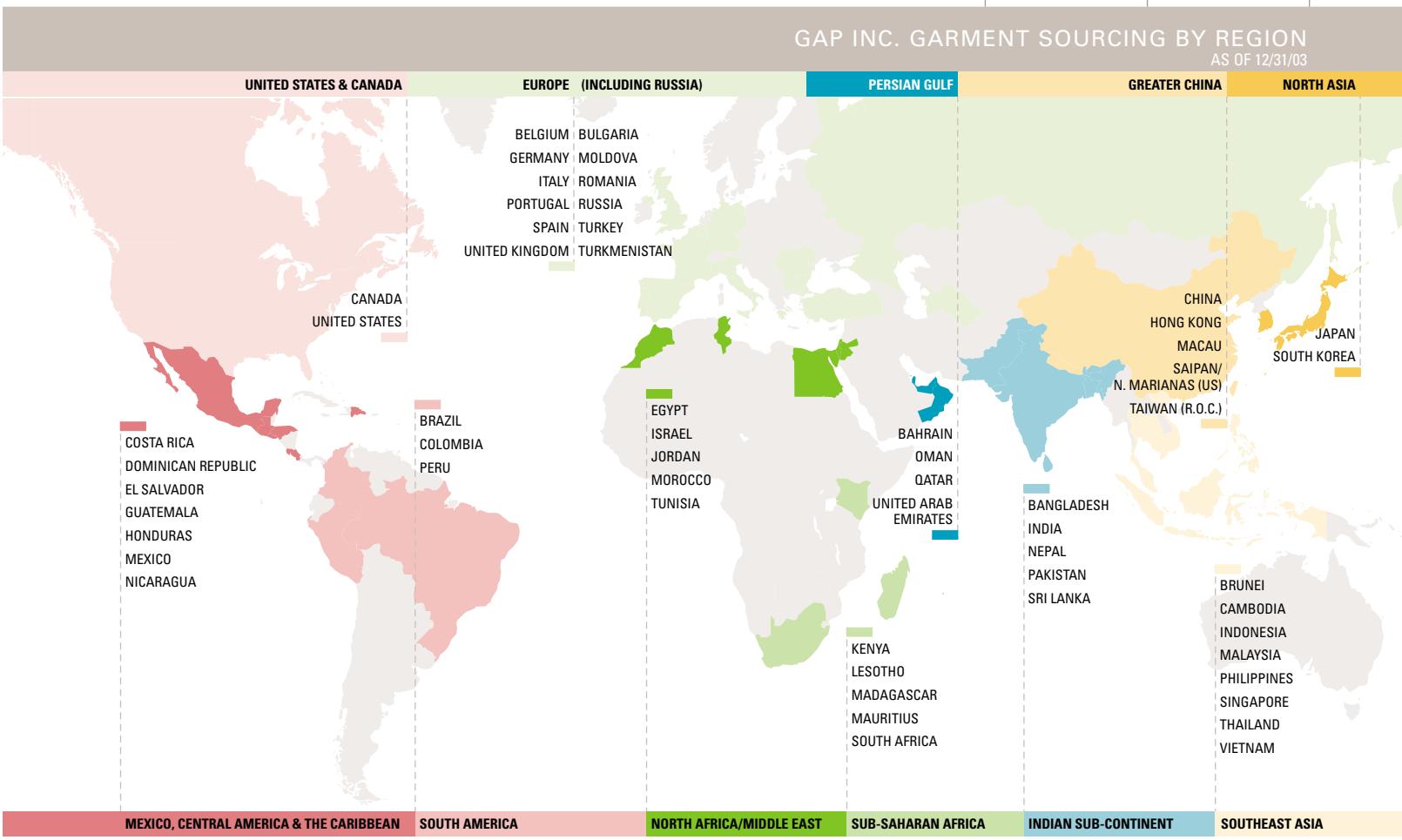
Corporate Compliance and Governance

- Nine of 13 members of Gap Inc.'s Board of Directors are independent directors
- Board has specific oversight function for social responsibility through Board's Governance, Nominating and Social Responsibility Committee
- Code of Business Conduct hotline to report concerns about Gap Inc. business practices: 866-Gap-Code in the U.S., Canada and Puerto Rico (toll-free); 770-582-5221 elsewhere (operator-assisted free call); email: corporate_compliance@gap.com

For more information about Gap Inc. and our social responsibility efforts please visit us at gapinc.com.

*In January 2004, Gap Inc. announced that it will exit the German market in August 2004, closing 10 Gap store locations, and focus resources on stronger international growth opportunities.

**As of April 13, 2004.



PRODUCTION OF THE REPORT

Because of some of the unique reporting challenges in the apparel retail industry, our first social responsibility report does not follow established general reporting standards, such as the Global Reporting Initiative (GRI). However, we have tried to cover key issues and areas important to our stakeholders. We will continue to evaluate reporting standards such as the GRI, and will seek to incorporate relevant standards into future reporting.

For the production of this report, we selected an environmentally responsible printer that has a "zero landfill" policy, recycles all process material waste and has an enclosed printing facility with negligible fugitive emissions.

This report was printed in the U.S.A. on recycled paper.
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Photography: Cover, Pages 2, 12, 13, 17, 24, 25 photos © 2004 Luis Ascui; Cover, Pages 2, 10, 11, 12, 17, 20, 21 photos © 2004 Sacha Dean Biyan; Cover, Pages 4, 13, 17, 26, 27 photos © 2004 Katarina Hesse; Pages 2, 6, 9, 38 portrait photos © 2004 Eric Millette; Cover, Pages 4, 12, 17, 22, 23 photos © 2004 Brent Stirton.
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Banana Republic
Old Navy

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