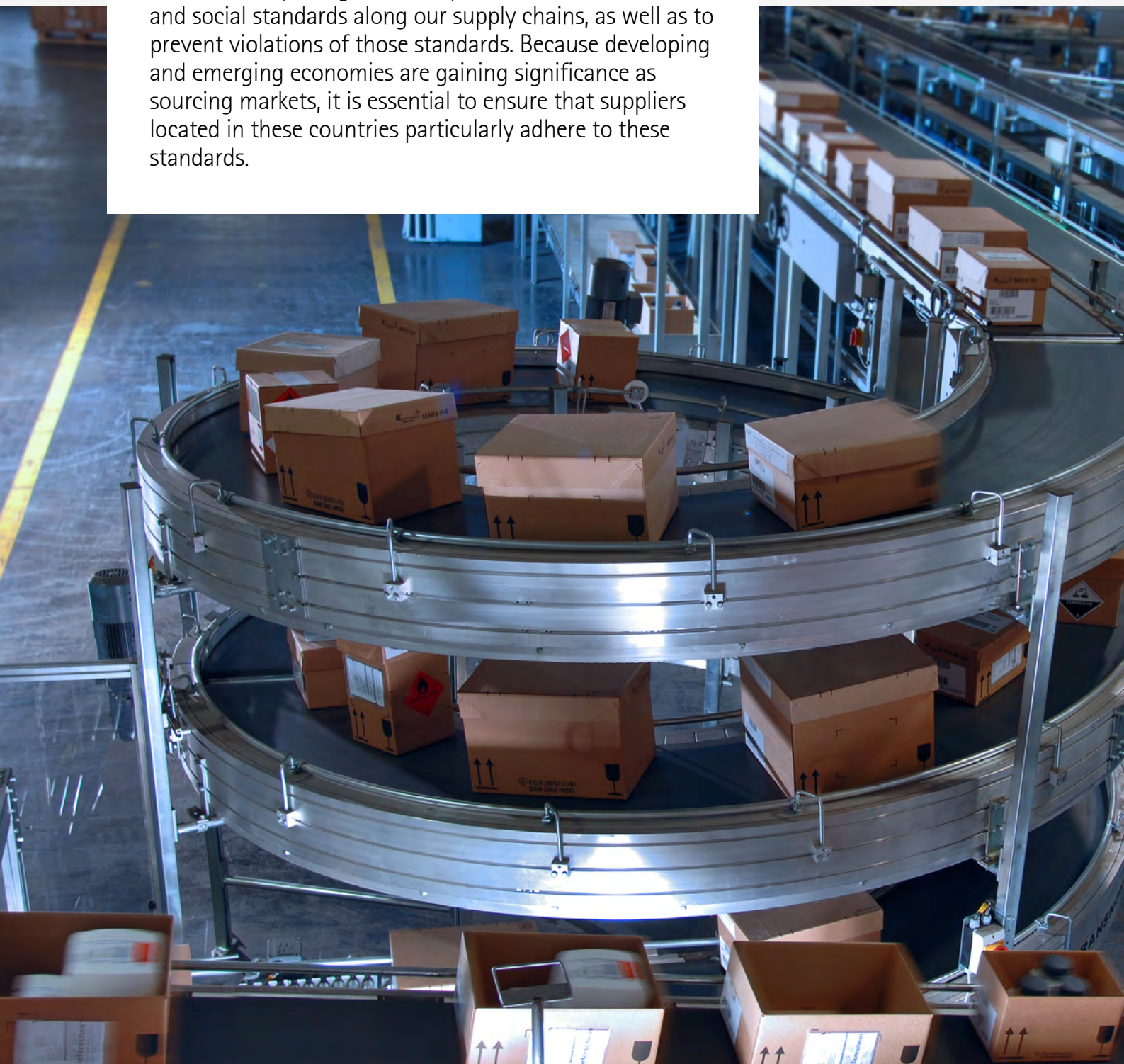


Suppliers

Merck's supplier management focuses on more than just typical sourcing priorities such as competitive pricing, quality and delivery reliability – for us, compliance with fundamental environmental and social standards is also a key strategic goal. With this in mind, in 2013 and 2014 we further optimized our procurement strategies, processes and guidelines, aiming to improve adherence to internationally recognized compliance, environmental, and social standards along our supply chains, as well as to prevent violations of those standards. Because developing and emerging economies are gaining significance as sourcing markets, it is essential to ensure that suppliers located in these countries particularly adhere to these standards.



Supplier management

Our Group function Procurement is responsible for integrating corporate responsibility (CR) with our sourcing and supplier management processes. An office within Group Procurement coordinates all corresponding measures, such as revising our guidelines and processes, or joining the Together for Sustainability chemical industry initiative. Through reporting lines and the Merck intranet, our Procurement employees in all countries receive information on the guidelines and measures used to ensure compliance with our supply chain standards.

Procurement guidelines

Our fundamental expectations for suppliers and service providers include their compliance with fundamental environmental and social standards that are derived primarily from the International Labour Organization Core Labor Standards and the UN Global Compact. To this end, we have been supporting the Compliance Initiative of the German Federal Association for Materials Management, Purchasing and Logistics (BME) since 2009 and have additionally signed the BME Code of Conduct. This document contains essential rules for combating corruption, violations of antitrust law, and child labor, and features principles on promoting human rights, environmental protection, human health, and fair working conditions.

Through our "Group Procurement Policy", updated in 2013, we ensure that our procurement processes adhere to CR standards. These processes cover everything from selecting to assessing and monitoring our vendors and service providers. This policy reflects numerous internal and external guidelines, such as the Merck Code of Conduct, the Merck Human Rights Charter, our Corporate EHS policy, ISO 14001, and the BME Code of Conduct.

To complement our procurement policy, we drafted the "Merck Responsible Sourcing Principles" and integrated them Group-wide into our general terms and conditions in 2013. These principles define what we require of our suppliers with regard to corporate responsibility, obligating them to apply our corporate responsibility standards to their upstream value chain.

Supplier monitoring

A key element of our supplier management process is ensuring that our suppliers implement CR standards, as well as monitoring their compliance. For this reason, we introduced an IT system in 2013 that utilized a structured questionnaire to collect self-reported information from suppliers. After deciding to join the Together for Sustainability (TfS) initiative, we discontinued this system because the initiative's EcoVadis® platform provides extensive supplier assessments.

The TfS initiative, founded in 2011 by companies in the chemical industry, aims to systematically assess and improve sustainability sourcing practices, including ecological and social aspects. Suppliers are assessed either on self-reported and publicly accessible information, or on information obtained during audits. The evaluation results are utilized by member companies, who abide by all restrictions stipulated by competition law. Beyond evaluations of the suppliers we have selected under our risk-based approach, we thus also have access to evaluations and audit results for other vendors who work for us.

In the course of 2015, we will be switching our supplier CR assessments and CR audits to the TfS method and integrating the TfS database into our supplier management system. We are planning to start conducting assessments and audits according to this new procedure in 2015.

Sustainability audits

In addition to collecting self-reported supplier information, Merck also conducts CR audits on select vendors based on the potential risk they pose. These audits are based on the corresponding company standard. Suppliers are assigned a risk category based on the risk levels in their country, the product category, and the share of their sales that come from Merck. In general, we assign vendors from non-OECD countries to a higher risk category. Regardless of their OECD status, suppliers are also audited if there are indications that they have failed to comply with our requirements.

All deviations from the "Merck Responsible Sourcing Principles" or from national statutory requirements identified in the course of an audit are classified as either critical, major or minor. The audit results as well as any corrective action required are communicated to the vendors via an audit report. When an audit reveals defects in a supplier's processes and conduct, we require them to provide us with a corrective action plan that describes the

course of action needed to address the issues. When it comes to defects that are classified as critical or major, we check whether the appropriate corrective action has been taken. For critical defects in particular, we consider the option of terminating business relations if the problems are not sufficiently rectified. The audit team additionally determines how often follow-up audits need to be conducted.

Defect classification

- **Critical defects:** Any defect rated as critical must be rectified or mitigated as soon as possible. The supplier must submit a corrective action plan to Merck within one week of receiving the audit report.
- **Major defects:** For major defects, the supplier must submit a formal corrective action plan within one month of receiving the audit report.
- **Minor defect:** Minor defects do not require a formal corrective action plan, nor will we monitor the implementation of the corresponding corrective actions.

In response to the results of our risk assessment, a total of 49 CR audits were conducted in 2013 and 2014, either by us or by a service provider. We found critical defects at 16 suppliers, and major defects at 40 suppliers. For 26 of the vendors with critical or major defects, the issues had to do with their ecological impacts, in particular stemming from waste and hazardous material storage at their facilities. In addition to this, we also identified 40 suppliers who exhibited flawed work practices, primarily in terms of occupational health and safety. Neither our audits nor the self-reported supplier information revealed significant risks regarding violations of the right to assemble or engage in collective bargaining, nor with regard to child labor, forced labor or compulsory labor.

In 2013 and 2014, our CR audits focused particularly on our mica suppliers in India, 14 of whom were audited within this period. We terminated our business relations with two of our vendors because they failed to carry out the required corrective action in a satisfactory manner.

We aim to cultivate long-term working relationships with our direct suppliers. To this end, we conduct workshops in order to help them comply with our standards as well as to develop and grow. We held one vendor workshop in China in 2013 and one in 2014. In addition to focusing on quality assurance, the training also covered our CR and EHS standards. Merck is furthermore involved in the local and regional supplier workshops organized by Together for Sustainability (TfS). One such workshop was held in China in 2014, and TfS is planning to host an event in Brazil in 2015.

Reporting violations within the supply chain

Via our central SpeakUp Line, our employees can report compliance violations as well as violations of CR standards that occur within our supply chain. In the 2013-2014 period, we received no such reports. We do not have a formal procedure for handling reports from outside of the company, nor do we currently have plans to establish one.

Goals: Supplier management

Goal	Action	By?	Status in 2013 and 2014	Status
Ensure our suppliers adhere to ethical, social, environmental, and compliance standards (part of our "risk mitigation" strategic procurement objective)	Conduct 20 CR audits on high-risk suppliers in 2014	End of 2014	In 2014, we conducted 24 audits on high-risk suppliers.	—
	Systematically collect self-reported supplier information	End of 2013	We have set up an IT system and received the first set of self-reported supplier information. This system has been discontinued because we are instead integrating the TFS database into our supplier management system.	—
	Join the Together for Sustainability (TfS) chemical industry initiative	End of 2014	We held workshops to prepare employees and joined the TfS Initiative in mid-2014.	—
	Conduct workshops to prepare Merck to integrate into the TfS program			
	Systematically collect self-reported supplier information in line with the TfS methodology	End of 2015	We are implementing the TfS methodology for supplier assessments and audits, as well as for tracking them.	+
	Establish a CR standard operating procedure	End of 2015		+

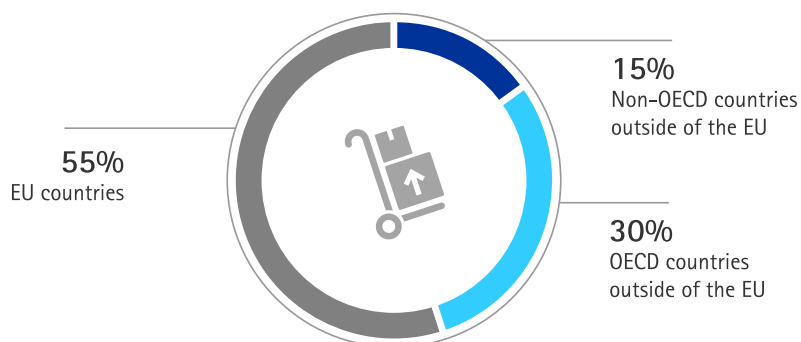
Legend: — Achieved — In progress — Not achieved + New goal

Supply chain

We procure the raw materials, packaging materials, technical products, components, and services we need from over 60,000 suppliers across more than 130 countries. All goods and services purchased in 2013 totaled € 4.1 billion, with € 4.3 billion in 2014.

Of the goods and services (including R&D services) purchased in 2014, we purchased 55% from suppliers based in EU countries and 30% from vendors in OECD countries outside the EU. The share of goods and services sourced from non-OECD countries outside the EU rose from 12% in 2012 to 15% in 2014.

2014 Procurement volume (%)



These figures make it clear that emerging economies are playing an increasingly important role in Merck's sourcing activities. One major reason is that certain pharmaceutical products are being produced in the developing and emerging countries in which they are commercialized. For instance, the medicines we manufacture in India, Pakistan and Indonesia are intended for those markets. This approach reflects our Access to Health strategy and is also stipulated by local law. For our products to be manufactured locally, we require compliance with our quality and safety standards; the same goes for the transfer of our technology, skills and intellectual property. All of Merck's pharmaceutical products, whether for developed or developing markets, are produced in manufacturing plants that meet global Good Manufacturing Practices (GMPs).

Merck has no internal guidelines stipulating that local suppliers are to be given preference in the contract award process. However, there are cases in which local vendors have a competitive advantage owing to their proximity, for instance when it comes to the purchase of technology or packaging materials. Furthermore, local legislation sometimes requires us to use local vendors, especially in the pharmaceutical industry. Otherwise, we source our goods and services globally, depending on availability and supply.

Responsibility in the mica supply chain

Merck utilizes mica from India as a primary raw material for effect pigment production. This special mica has properties that are necessary for the manufacture of top-quality pigments. In the course of an investigation in 2008, we discovered that at the start of the supply chain, mica is sometimes collected by children, generally together with their parents. This is not compatible with our corporate values, nor with the principles of our Human Rights Charter.

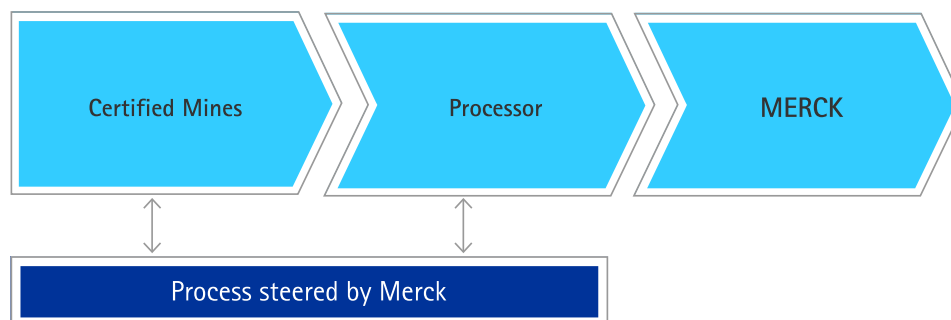
Merck takes a firm stance against child labor. As a signatory to the United Nations Global Compact, we are actively fighting to end this practice. We require our suppliers to act accordingly and contractually prohibit them from utilizing child labor.

As a result of our 2008 supply chain audit, we have realigned the mica supply chain in order to prevent child labor and to ensure that vendors comply with the principles of our Human Rights Charter. Since then, we have been sourcing only mined mica. We no longer use any mica that is collected because, in this informal work environment, we cannot guarantee that child labor is not being used. However, we consider it important to maintain our business relationships with suppliers in the regions where mica comes from and thus safeguard jobs in Jharkhand, a region in northeast India plagued by poverty and political uncertainty. This is why we maintain direct business relationships with our partners along the mica supply chain, meaning the mica mine operators and the mica processing plants. We have set up an office in the region; our staff there are in close contact with our business partners, whom we have instructed on our values, along with the social and environmental standards that we expect of them. Mine owners and processing plants accept their responsibilities and help us keep the mica supply chain free of child labor.

In addition to these measures, we have also set up a mica tracking system in order to guarantee that the raw materials supplied to Merck come exclusively from mines and not from uncontrolled sources. In order to track the mica flow, owners maintain a daily log of the amount produced by their mines. It is unlikely that mine owners would falsely reported inflated production figures for the individual mines and then make up the difference with mica from uncontrolled sources. After all, such a course of action would incur additional licensing fees that would then have to be paid to the government. Merck crosschecks the final amounts once a month.

On top of this tracking system, we have also developed an audit system that entails surprise audits conducted by Merck or third party partners. This system aims to ensure that the mines and processing plants are complying with our requirements for environmental protection, safety, and working standards. Once a month, a local organization investigates the working conditions and standards in the mines. In addition to this, an international organization also conducts an annual audit that reviews both working standards, as well as environmental, health and safety standards. The audit reports indicate all issues identified and specify corrective action. Our employees in Jharkhand check whether the required corrective action has been taken.

Mica supply chain



In 2013 and 2014, we conducted 14 audits on our mica suppliers that were part of the standard yearly audit process. Around three-fourths of the corrective actions specified in the previous audits had already been taken or were underway when the audit was performed. Because they failed to carry out the corrective actions in a satisfactory manner, we terminated business relations with two of our vendors.

Social engagement along the mica supply chain

Apart from our strategy to guarantee oversight of the entire mica supply chain, we are working together with the IGEP Foundation to better the living conditions of the families in the mica mining regions of India. We are therefore financing three schools with daycare centers as well as a vocational training center for tailoring and carpentry. These schools now have an enrollment of around 500 children. At a fourth school opened by one of our mica suppliers in 2014, Merck furthermore provides scholarships for 100 children.

We are improving medical care in the region through a local wellness center that is operated by the IGEP Foundation. This facility has a doctor and a nurse on duty every day and is highly appreciated by the region's 20,000 inhabitants, who previously had no health care at their disposal. The doctor and nurses also pay visits to schools and villages in the vicinity.

From 2010 until 2013, we partnered with the Indian non-profit organization Bachpan Bachao Andolan to develop 20 "child-friendly villages" in Jharkhand. This three-year

project aimed to improve understanding for children's rights and foster the basic conditions for children to regularly attend school. In collaboration with local communities, civil servants, and teachers, the project has made visible progress.

Stakeholder dialogue on the mica supply chain

Since the start of our supply chain changeover, we have been keeping interested customers and other stakeholders regularly informed on the progress made on mica sourcing as well as the associated projects. Employees in our Jharkhand office are in communication with our project partners and other stakeholders, such as local and federal agencies.