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The Coca-Cola Co. (KO)

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MANAGEMENT DISCUSSION SECTION

Operator: At this time, I'd like to welcome everyone to The Coca-Cola Company's Third Quarter Earnings Results Conference Call. Today's call is being recorded. If you have any objections, please disconnect at this time. All participants will be on a listen-only mode until the formal question-and-answer portion of the call. I would like to remind everyone that the purpose of this conference is to talk with investors, and therefore questions from the media will not be addressed. Media participants should contact Coca-Cola Media Relations Department if they have any questions.

I would now like to introduce Mr. Tim Leveridge, Vice President of IR and FP&A. Mr. Leveridge, you may begin.

Timothy K. Leveridge

Vice President, Investor Relations Officer & Head-Financial Planning & Analysis, The Coca-Cola Co.

Good morning and thank you for joining us today. I'm here with James Quincey, our Chairman and Chief Executive Officer; and John Murphy, our Chief Financial Officer. Before we begin, please note we've posted schedules under the Financial Information tab in the Investor section of our company website at www.cocacolacompany.com. These schedules reconcile certain non-GAAP financial measures, which may be referred to by our senior executives during this morning's discussion to our results as reported under generally accepted accounting principles. You can also find schedules in the same section of our website that provide an analysis of our gross and operating margins. In addition, this conference call may contain forward-looking statements, including statements concerning long-term earnings objectives and should be considered in conjunction with cautionary statements contained in our earnings release and in the company's most recent periodic SEC report.

Following prepared remarks this morning, we will turn the call over for questions. Please limit yourself to one question. If you have more than one, please ask your most pressing one first and then reenter the queue.

Now I will turn the call over to James.

James Quincey

Chairman & Chief Executive Officer, The Coca-Cola Co.

Thanks, Tim. And good morning, everyone. After a strong first half of the year we saw continued momentum in our business in the third quarter. While the global recovery remains asynchronous, our people and our systems are leveraging the learnings to deliver good results and emerge stronger. And while markets are at different stages of re-opening around the world, our local businesses have been increasingly resilient through restrictions and lockdowns. As a result, our underlying volumes have accelerated on a two-year basis with quarterly growth versus 2019 for the first time since the pandemic began.

This improvement has been supported by our transformation agenda, which set us on our path to more efficient and effective marketing as well as more disciplined and intelligent innovation. We're investing accordingly behind our portfolio of loved brands and are seeing signs of early traction. Given strong results year-to-date, and increased visibility into the rest of the year, we expect to deliver organic revenue at the high end of our previously provided range and are raising bottom line and cash flow guidance for the full year. This morning, I'll provide a business update and discuss how our networked organization is executing well in this dynamic environment. Then John will discuss our financials and raised guidance, and some early considerations for 2022.

In the first half of 2021, mobility and business levels improved in many markets as lockdowns eased and vaccinations increased. The recovery has not been a straight line and continues to be uneven around the world. But despite the asynchronous recovery, in the third quarter, our volumes surpassed 2019 levels for the first time since the pandemic began. Although not yet back to 2019 levels as a percent of our business, we saw sequential improvement in away-from-home volumes on a two-year basis as consumers returned to many of their former routines. At-home volumes also showed ongoing strength even as away-from-home channels improved.

The quarter was off to a promising start in July, but the Delta variant impacted several markets resulting in a softer August, followed by improvements in September as the variant began to lessen in some of our key markets. But the pandemic continues to be a key factor across our operating environment in addition to the ongoing pressure points in our supply chain. However, our networked system is leveraging the learnings from the past 18 months, sharing best practices and skillfully executing by applying revenue growth management and working our supply chain levers to capitalize on the strength of our brands and mitigate disruptions. The industry is growing, and we continue to gain share. Our overall value share improved year-on-year and remains above 2019 levels. We're pleased to report gains across categories as well as both within at-home and away-from-home channels. Our operating units are combining the power of scale with the deep knowledge required to win locally in an environment that remains dynamic.

So, diving a little into the key drivers across our geographies, starting with Asia Pacific. In China, media investments across categories are yielding promising signs. Results in the quarter reflect strict COVID lockdowns and some weather-related disruption in August, while September marked sequential improvements. Japan's state of emergency was lifted at the end of the quarter after consumers spent the majority of 2021 in lockdown. Strength and execution across our teams and innovation has helped lessen impacts, and our consumer base has grown beyond 2019 levels. In India, we participated strongly in the recovery by focusing on affordability and omni-channel growth through e-B2B. We grew both trademark Coke and local icon Thums Up using effective marketing activations. We had share gains in ASEAN and the South Pacific operating units despite pandemic-related restrictions in all of its top markets. Our investments behind Sparkling flavors and Coca-Cola Zero Sugar will continue to create value when lockdowns are lifted.

In EMEA, in Europe, we gained value share across nearly all categories as restrictions eased. While weather, a slower recovery in tourism and the Delta surge had an impact, our global campaigns for key brands including Coca-Cola Zero Sugar, Sprite and Fanta helped drive Sparkling share. As vaccinations accelerated in Eurasia and the Middle East, we maintained momentum through effective revenue growth management initiatives, resulting in top line that expanded faster than the macro environment in those top markets.

Our results in Africa were balanced across regions and categories during this quarter despite a third wave of the pandemic that resulted in targeted lockdowns. Vaccination rates remain on the low side relative to the rest of the world, and our focus remains on affordability and single-serve packs as mobility increases in countries like Egypt and Nigeria.

We maintained strong momentum in North America despite the COVID resurgence in many states leading to stalling consumer sentiment and supply chain challenges that resulted in both missed opportunities and incremental costs. The at-home channel remains healthy, and although away-from-home growth accelerated early in the quarter, labor shortages have constrained capacity with some on-premise customers. Recent price actions to offset higher input costs have been effective, with lower than expected price elasticity to-date, and promotional levels remain below 2019.

In Latin America, successful commercial initiatives, including affordability packs, increased availability of our key products and strong customer execution in both modern and traditional trade drove volume growth across all major markets amidst an improving COVID environment. Improvement in single-serve mix, some pricing actions and connecting brand strategies to on-premise customers to drive further recovery in the away-from-home channels all contributed to strong price mix.

In Global Ventures, Costa benefited from retail store recovery as the UK reopened. With improved reach and frequency from its enhanced loyalty program, Costa continues to expand across platforms into new markets in partnership with our bottlers, resulting in growing brand awareness.

Our Bottling Investments Group performance was driven by India and the Philippines. BIG saw strict lockdowns in several markets as well as rising inflation but has continued to see share gains year-to-date in South Africa. Adverse impacts have been well managed through package and category mix improvements along with cost controls, preserving progress on our operating margins during the pandemic.

Global category teams are working with our operating units to build an engine to drive effective marketing at scale and innovation which will be amplified across the world. Highlights in this quarter include Coca-Cola Zero Sugar's new recipe has rolled out in more than 50 countries and has had accelerated growth in the last three months. In September, trademark Coca-Cola's new global brand philosophy, Real Magic was unveiled, featuring a refreshed look for our iconic logo, The Hug. The Real Magic platform takes a digital-first approach, and our execution feature a range of experiences that are tailored to Gen Z and leverage passion points like gaming and music to attract a new generation of drinkers.

Sparkling flavors gained share in the quarter, driven by investments in targeted brand county combinations with a focus on occasions and Zero Sugar offerings. In China, Sprite volume growth was accelerated by leveraging the global Let's Be Clear campaign during summer music festivals. Similarly, the What the Fanta campaign focuses on snacking and it's driving growth across all key metrics in Europe.

The Hydration, Sports, Tea and Coffee categories are seeing a good return on spend behind global brands. AHA's expansion into new markets this year has shown flexibility to adapt to local customer and consumer needs. In Advanced Hydration, functional benefits have helped to stretch brand power and drive share for Aquarius as it becomes more of a global brand. Tea and Coffee have had success with Fuze Tea in Europe and both Ayataka and Costa Ready-to-Drink in Japan. There is an opportunity to recover share in Georgia Coffee as the at-work occasion returns.

Our Juice portfolio gained share this quarter, helped by Minute Maid Pulpy performance in China, Del Valle growth in Latin America and strong results across brands in Africa. In Dairy, fairlife is set to become the first \$1 billion brand in our Dairy portfolio and has recently launched its joint venture in China. Our experimentation with Topo Chico Hard Seltzer is expanding, and we're gathering valuable insights globally, including the importance of building the category in regions where it is nascent. We are seeing encouraging performance where the flavored alcoholic beverage category is growing rapidly, and we have on-self presence. Molson Coors recently announced a national rollout of Topo Chico Hard Seltzer in the US with new margarita flavors. We also recently announced an expansion of our relationship with Molson Coors to bring the brand into Canada.

As the pandemic recovery has progressed, we've seen challenges and disruptions in many parts of the world in addition, to inflationary forces that could persist. We have years of experience in dealing with these types of environments and are enhancing our strong capabilities that enable us to do so. We are using the crucial tool of revenue growth management in its many forms and are executing in collaboration with our bottling partners. We

continue to refine our ability to optimize price and package offerings according to occasions, brands and channels, striking the right balance between premiumization and affordability.

In addition to streamlining our portfolio, targeting more disciplined innovation, intelligent experimentation and transforming our marketing model, we're also building strong digital capabilities. We have taken an enterprise approach and are progressing on the rollout of multi-category e-B2B platforms with our bottlers globally. As an example, Wabi is seeing strong growth outside its home market of Latin America and has more than 50 categories contributing meaningfully to its sales on the platform. Additionally, we are delivering outsized growth through a powerful and growing omni-channel presence across regions. We're driving incremental instance with partners like food service aggregators. North America, for example, has grown attachment rates by mid-single-digits with third party and restaurant-owned platforms. And we're gaining share in e-commerce with significant wins in Eurasia and hitting record levels in Latin America this quarter.

I'd also like to reiterate that sustainability is an integral part of our business strategy and is a key driver of future growth. From 2018 when we launched World Without Waste to today, we've made much progress against our pillars to design, collect and partner to deliver against our goals. Our commitment to reduce waste globally is also closely connected to our climate ambitions because collecting more empty packages, using more recycled material, light-weighting our bottles and using plant-based materials are all ways we are embracing the collective efforts to decarbonize the global economy. We strive to provide stakeholders with clear progress against our goals through our annual business and ESG report and our World Without Waste report, including using the global reporting initiative, FASB and TCFD reporting frameworks as well as disclosures through other publicly available avenues like CDP and the Ellen MacArthur Foundation.

We continuously revisit our ESG reporting and disclosures to ensure our leadership position. We do not take our responsibility lightly, and we carefully and thoroughly vet long-term objectives with our system partners and only commit to new goals with a clear actionable plan. To ensure we remain transparent and respond to this evolving landscape, we'd like to invite you to join us for our virtual ESG event on November 3, where key business and sustainability leaders will provide an update on our initiatives and answer your questions.

As we look at our year-to-date performance of the system, it's clear that we are emerging stronger from the pandemic, delivering solid results under a more networked structure. Now, I'll turn the call to John to discuss our third quarter results, our updated outlook and some initial thoughts about 2022.

John Murphy

Chief Financial Officer & Executive Vice President, The Coca-Cola Co.

Thank you, James. In the third quarter, we delivered another set of strong results, building on the momentum we've seen this year. Our Q3 organic revenue was up 14%, with concentrate shipments up 8% and price mix up 6%. Price mix was led by strong pricing in North America and Latin America and further improvement in away-from-home channels in many markets. Unit case growth was 6% with absolute unit cases ahead of 2019 levels for the first time this year and a sequential improvement versus the second quarter on a two-year basis. Concentrate shipments outpaced unit cases in the quarter due to inventory build by some of our bottling partners to manage through near-term disruption. Comparable gross margin for the quarter was up approximately 160 basis points versus prior year, driven by pricing in the markets, positive mix and timing of shipments. Despite some pressure points in the supply chain, we're successfully pulling the levers at our disposal to mitigate impacts to the best of our ability.

We continue to invest as many markets reopened during the quarter and significantly stepped up our marketing dollars versus prior year. As a result, our comparable operating margin compressed by 40 basis points year-over-

year, more than offsetting the flow-through from the strong top line. In our operating income, we saw some leverage come through from the other income line and a lower tax rate for the quarter that was driven by our updated effective tax rate for the full year to 18.6% from 19.1% previously. Putting all of this together, third quarter comparable earnings per share of \$0.65 was an increase of 18% year-over-year including a 3-point benefit from currency. We also delivered strong year-to-date free cash flow of \$8.5 billion. Given our strong results and with one quarter remaining, we have good visibility and are raising guidance for the full year. We now expect to deliver organic revenue growth of 13% to 14%, which is at the high end of our previously-provided range, and comparable EPS growth of 15% to 17% in 2021.

Our updated guidance for free cash flow of approximately \$10.5 billion represents significant progress over the past few years and particularly during the COVID era. This progress is further dimensionalized as follows. We expect to achieve this year a dividend payout ratio below our long-term target of 75% of free cash flow for the first time since 2015. We anticipate delivering another year of free cash flow conversion above 100%. And finally, our expected free cash flow has almost doubled since 2017. Our improving cash flow position will allow us to be even more vigorous in pursuit of our capital allocation priorities: first and foremost, to invest in our business; secondly, continuing our track record to grow our dividend; thirdly, to seek opportune M&A; and finally, with excess cash to repurchase our shares.

So, as we think about Q4, a few things to keep in mind. One, the recovery phase looks different around the world, and we expect that to continue. Two, we continue to see a minimal commodity impact due to hedges we have in place for the remainder of the year. Three, from a marketing perspective, we expect to increase consumer-facing marketing spend toward levels similar to 2019 while improving the quality of that spend and allocating it in a more targeted manner. Four, our currency outlook continues to contemplate a tailwind of 1% to 2% at the top line and approximately 2% to 3% to comparable EPS in 2021 based on current spot rates and our hedge position. Last, but not least, our current full-year guidance has built in the leveling out of our concentrate shipments that are running ahead year-to-date due to timing, considering that we have six fewer days in the fourth quarter.

It's not typical for us to provide commentary on the year ahead at this stage, but I would like to highlight a few points regarding 2022, given the dynamics we are already seeing. While there are puts and takes to consider from the pandemic, looking into next year we're confident in the underlying top line trajectory, supported by our transformation work, our innovation agenda and a more efficient and effective approach to marketing. Along with this ongoing momentum in revenues, we also expect to see some higher costs. We are not immune to the commodity inflation that has been impacting the world for the better part of 2021, nor the rapidly changing environment. We've been successful with hedges that were put in place to mitigate the impact of input cost inflation, and those will begin to roll off in 2022. Based on current rates and hedge positions, we'd expect commodity inflation to have a mid-single-digit impact on our cost of goods sold in 2022. We've been proactively accelerating our revenue growth management and productivity levers to offset some of this pressure as we look out to next year, and we're closely monitoring the moving parts in the supply chain to ensure we are well-positioned to meet demand.

Moving to marketing dollars, we'll continue to invest purposefully in our brands and markets to support top line growth with spend more heavily weighted towards consumer-facing activity. Regarding currency, if we were to assume current rates and our hedge position, there would be an approximate 2 to 3 points currency headwind to revenue and a 2 to 3 point headwind to earnings for the full year of 2022. Of course, volatility remains, and several factors could have an impact on our currency outlook between now and February. Overall, as vaccinations continue to progress globally, we are in a better position today to navigate this environment, and we feel good about the potential for our business. We look forward to coming back with more specific guidance after the fourth quarter.

In closing, I'd like to acknowledge the more than 700,000 men and women of the Coca-Cola system whose tremendous dedication and hard work have been instrumental to delivering the strong results in the first nine months of the year. The alignment of our systems and its deft navigation through a challenging supply environment and an asynchronous pandemic recovery have been key enablers to emerging stronger. We're confident in our updated guidance and our ability to further leverage our strong capabilities to drive sustainable top-line growth and maximize returns.

With that, operator, we are ready to take questions.

QUESTION AND ANSWER SECTION

Operator: [Operator Instructions] Your first question is from the line of Bryan Spillane with Bank of America.

Bryan D. Spillane

Analyst, Bank of America Merrill Lynch

Hi. Thank you, operator. Good morning, everyone. I appreciate the commentary on the cadence through the quarter and even giving us a little bit of some pieces to look at 2022. But if we can just – I think, one of the questions we're getting now is just kind of the business momentum and maybe how it's come, progressed as we've moved into the fourth quarter. So, maybe if you could give a little bit more color on just how you're seeing the business currently? And also, just some perspective on how you see that momentum going into 2022, given not just the pandemic but also inflation and pricing? And so just to get some context about how the business is going so far this quarter, but also just your perspective on that going into 2022?

James Quincey

Chairman & Chief Executive Officer, The Coca-Cola Co.

Sure. Good morning, Bryan. Firstly, we clearly have been executing against our emerging stronger strategy. As you can see that coming through, we've called out that the third quarter was the first quarter to be growing versus [ph] fourth (25:02) quarter versus 2019. So, a sequential improvement as we've been going through this year from the first half, which was below 2019, to the third quarter, which was above it. So, clearly sequential improvement is coming through as we have adapted our ability to cope with the ups and downs of the lockdowns and the re-openings.

Now, in the quarter as you say, we called out that July started well and then August was softer as there were more lockdowns and then September was better. When you think about where that's going in the fourth quarter and into next year, I mean, clearly the fact that we have raised or clarified guidance on revenues to be at the top end of the range should lead you to feel confident that we see visibility in the downhill of the rest of this year. October has started strong and in line with expectations. So, we feel good that the momentum is there. I mean, I've made the caveat, as many other people have done through COVID, that who knows what could happen in the downhill with variants and with lockdowns. But at the moment what we see is the momentum is there. We feel good about our top-line guidance for the year, and October backs up that statement.

And then as it goes through 2022, obviously too early to call the full year next year and we will do so in February. But again, in the comments, in the press release, in John's comments, we said we feel that we have momentum in the business. Again, the caveats of who knows what will happen with variants and potential lockdowns, but we do see the world emerging from the crisis a bit like an earthquake. You get more aftershocks, but the consequent

aftershocks tend to be smaller than the early ones, and that's kind of how we see 2022. So, we feel there's good momentum and the strategy is working and it's getting us back on track.

Bryan D. Spillane

Analyst, Bank of America Merrill Lynch



Okay. Thank you.

Operator: Your next question is from the line of Lauren Lieberman with Barclays.

Lauren R. Lieberman

Analyst, Barclays Capital, Inc.



Great. Thanks. Good morning. I wanted to just talk a little bit more maybe about supply chain. Last quarter you talked about isolated pressure points and definitely offered commentary to say that you're able to tap into supplier relationships and so on. But I was just curious, I guess. A, what's the thought that bottlers continue to try to build inventory not just in advance of 4Q, but even looking into 2022 that you kind of maintain this disconnect between concentrate shipments and unit case volume? But also, to talk a little bit on the packaging side of things and what the system is able to do to have better access to the range of packaging options. Because things have been tight all year, but it sounds like they're getting worse. And so just curious what you could offer from what you guys are doing to be able to manage through that so well. Thanks.

James Quincey

Chairman & Chief Executive Officer, The Coca-Cola Co.



Sure, Lauren. Yeah, I'm not sure I used the word isolated last quarter, but I know what you mean. Look, firstly we have a lot of capability on managing through crisis. This may be a unique and global one, but most managers and leaders at Coke have some time in their career managed a part of the world or a country that's gone through severe dislocation. And so, we have built capability over the years to manage through this. And in particular, in the supply chains, organizations of the company and with the bottlers, and so we have strong capabilities. We look for long-term partnerships with the ecosystems, the supply chains, whether that's imports, materials, or logistics. We also act as a system in a number of regards. We have something called the Cross-Enterprise Procurement Group which buys key commodities on behalf of the company and the bottlers. So, there's a great deal of coordination between ourselves and the bottlers.

In terms of the problems, it's a bit like whac-a-mole. Things pop up. We've talked previously about can pressure in the US. Self-evidently there's issues in shipping and freight and availability of labor in places. Then you get one that pops up. The price of gas spikes in Europe and the availability of CO2 comes under pressure. There was a PET plant went offline because it burst into flames in Brazil, et cetera, et cetera. So, there is a heightened degree of sporadic problems appearing, as well as kind of structural shortages of certain ingredients. But we have global scale. We have global coordination, and we have long-term relationships with many of our ecosystem partners that are allowing us to manage and offset what's going on.

Now, as regards the bottler inventory towards the end of the year, clearly we're working with the bottlers. And obviously they can have the confidence and assurance that they don't necessarily need to hold it in their hands for us to be certain of having it as a system. We obviously ourselves being kind of the key player in providing the contract make sure we have enough buffered availability of ingredients and concentrate to make sure the bottlers are going to be in a good position, and we manage that accordingly with them in every year and particularly this one.

Operator: Your next question is from the line of Dara Mohsenian with Morgan Stanley.

Dara Mohsenian

Analyst, Morgan Stanley & Co. LLC

Q

Hey, guys. Thoughts around top line and volume recovery you mentioned earlier for 2022 were helpful. Can you spend a bit more time discussing the pricing environment that you're seeing also in the US, other developed markets and then in the developing markets? Obviously, we're seeing a pretty unique spike in commodity costs in terms of the magnitude. So, how is your system approaching pricing in this environment, given that unique level of increase? And specifically, for Coca-Cola itself, is the expectation that pricing can generally fully offset commodity increases on a dollar-for-dollar basis, ex any demand elasticity secondary impact, given you don't have as much commodity exposure as the entire system but share in the retail pricing moves? And then also maybe can you just detail the competitive pricing environment you're seeing from your key competitors? Thanks.

James Quincey

Chairman & Chief Executive Officer, The Coca-Cola Co.

A

I'm pretty sure that's additive – adds up to more than one question. But I'll give it a go, Dara.

Dara Mohsenian

Analyst, Morgan Stanley & Co. LLC

Q

Multi-part.

James Quincey

Chairman & Chief Executive Officer, The Coca-Cola Co.

A

Yeah. Multi-part. First point, we, as a matter of course, I mean, there's inflation every year. But we approach it from the point of view of going our brands need to earn the right to adjust their prices each year, whether that be because of the marketing, the innovation, the execution, the investment in the marketplace, or the pressure on COGS or the pressure on labor inflation. So, as you can see from our numbers, I mean, we are pulling all the levers of price and mix and marketing innovation each and every year. And so that is the starting point as we think forward into 2022.

Secondly, we see the environment of pricing, the example of the US and largely everywhere else as pretty rational, whether that be what competitors are doing or what the retailers are doing with their own label brands. And so, we see our approach as earning the right to take the price that creates value for ourselves, the system and creates value for the retailers and creates value for the consumers. And that's our starting point. Yes, we did take an off-cycle increase in the US. Obviously slightly different by brand and by pack, but certainly in the high single digits starting in August. The elasticity has worked perhaps a little better than they were last time. You may remember, whatever it was, four or five years ago, we took an off-cycle price increase in the US when there was a very strong adjustment in the logistics market in the US that caused everyone a great deal of problems. And so, we passed that through this time, and we will be looking at exactly what level our pricing needs to be for 2022. But again, the COGS input, the COGS push-through is a piece of the puzzle, and we certainly intend to earn the right to take the pricing for the brands and the packaging [ph] moving on (34:31).

And that is true in other parts of the world, I mean, obviously depending in emerging markets on the level of inflation in the marketplace, you've got some double-digit inflation places where there might be more than one price increase during the year. But in the other developed markets, again, you see this approach of earning the right to take the price based on the brand, the pack, the occasion, the channel and really driving that through.

Operator: Your next question is from the line of Steve Powers with the Deutsche Bank.

Steve Powers

Analyst, Deutsche Bank Securities, Inc.

Q

Hey, thanks. And good morning. Maybe pivoting back to volume for a minute, you mentioned obviously that 3Q volumes finished ahead of 2019 for the first time since the pandemic started, which is obviously a happy achievement. I guess what I'm wondering is if there's a way to sort of frame where 3Q volumes finished indexed to 2019 in terms of at-home versus away-from-home or future consumption versus immediate consumption. I guess I'm trying to get a better sense conceptually of how much further runway there may be in the away-from-home, I mean, the consumption side of the business recovering, which obviously has both volume implications but also beneficial price-mix implications. Is there a right way to frame – a right way to think about that from your perspective?

James Quincey

Chairman & Chief Executive Officer, The Coca-Cola Co.

A

Yeah. Sure. [indiscernible] (35:57) Q3 is above 2019 in volume. If I look at the mix of the business between away-from-home and at-home, the away-from-home has not yet recovered to the same share of mix that it was in 2019. And so of course implicit in your questions is, is that a tailwind going forward as more of the away-from-home recovers because of either the package or the brand or the occasion that it's related to? And the answer in some extent is yes. Now, worth bearing in mind but it's not a snapback, which is what you're seeing. It's not just a function of lockdown and when the lockdown ends the away-from-home comes back. I think, we're seeing an evolution of the landscape. You're going to see some, of course, away-from-home is a series of – a whole set of sub-channels. You're going to see some of those sub-channels where actually over the last two years, almost two years now, there's been a reduction in the number of outlets, and so our hypothesis is it will take time to see those outlets re-expand, reappear and so it won't – just because the lockdown ends, doesn't mean the outlet reappears. So, we'll see some of that. But of course, there'll be some channels that are not yet fully opened. Much of travel and kind of hospitality, there are a whole series of subchannels that are still running far below their 2019 levels.

So, yes, it's a headwind – it's a tailwind going into the future, but it's not dependent just on the end of lockdowns. And I think it will – if you imagine a curve, we've got – the snapback has happened and now it's going to be a little more of a smoothing of the curve to recover the rest of the away-from-home. Because in part people's habits have changed. Like I said, it's an evolving landscape. I mean, what degree of more permanent at-home work here are we going to see? Not quite clear. So, I think, we've got a big piece of it, let's say, half of it back of the mix, and there's another half to come. But it won't come overnight. It'll come over time.

Steve Powers

Analyst, Deutsche Bank Securities, Inc.

Q

Perfect. Thank you.

Operator: Your next question is from the line of Nik Modi with RBC Capital Markets.

Nik Modi

Analyst, RBC Capital Markets LLC

Q

Yeah. Good morning, everyone. James, I was hoping you can kind of give us an update on the reorg and all the changes that were made. I mean, do you have all the right people in the right seats now? And how is the organization adjusting to kind of the new decision-making matrix, if you could just provide us an update there? Just some of the feedback that I've gotten is that you still have some bugs being worked out. So I'm just trying to

get a better understanding of timing on when you think you'll kind of be optimally running under this new networked structure.

James Quincey

Chairman & Chief Executive Officer, The Coca-Cola Co.

I'm not sure I would ever call us arriving at the destination of optimally running. Because by the time we get there, something else will have changed in the world and we'll need to make some tweaks and evolve. Certainly, we stood up the organization in the first quarter, and then – and it was off to a good start. It's very much on track with our expectations. As you say, one would expect there to be some bugs and some kinks that need to be worked out, and that is what we're going through at the moment. And it's not that all of the change has happened yet. We've been running a – Manolo and the marketing team have been running a big agency review through this year. We're coming up on the final decisions on that in the fourth quarter, which will start bringing a structural amount of change next year in the way we interact in our marketing kind of the enabling spend ecosystem. So, there will be more change and we will continue with that. So, we're focused on working out the bugs of the bits we've already stood up and we'll be bringing more change in terms of how we get the marketing sorted out next year.

And I'm sure things will happen in the marketplace that will cause us to want to make further evolutions. But we certainly see that the early signs of how the new organizational model could help us both deal and manage through the crisis, whether it's what we've done on the supply chain or the procurement, but also set us up. Ultimately this is all about being an enabler to give us confidence in driving and delivering on our long-term growth algorithm.

Operator: Your next question is from the line of Bonnie Herzog with Goldman Sachs.

Bonnie Herzog

Analyst, Goldman Sachs & Co. LLC

All right. Thank you. Good morning, everyone. I was actually hoping you guys could talk about whether or not you have a competitive advantage during a period of rising input and transportation costs relative to your peers, given your asset light or asset right re-franchise model. I guess I'm thinking about this in context of your preliminary outlook for FY 2022 as it relates to COGS pressures. And then curious to hear I guess how you're working with your bottlers who really are experiencing pretty sharp cost pressures to essentially help them navigate through this tough environment. Thanks.

James Quincey

Chairman & Chief Executive Officer, The Coca-Cola Co.

Yeah. Let me start with the system view and then work back towards the company. Obviously, we're working with the bottlers on a collective basis and an individual and country basis. And I draw this distinction because on a collective basis, as I mentioned earlier, we have a unit called the Cross Enterprise Procurement Group which works on behalf of the system globally – us and the major bottlers – to procure the key input costs, whether it be resin, aluminum, sweeteners, whatever it would happen to be. And that's not just about buying. It's about the hedges and the pricing and the security of supply. So, there's a tremendous activity and coordination with the bottlers on the principal input costs. Then of course we work locally with the bottlers in the countries, taking into account all the other factors that go into how we might want to approach pricing, whether that's the other cost, the more local costs, the logistics, labor, et cetera, et cetera, and our agenda for marketing and innovation and execution, RGM, and come up with a plan to make sure that we drive that into the marketplace and that the

brands earn the right for the pricing that keeps them attractive to the retailers, attractive to the consumers and drives the business for us.

And then obviously within that, the company itself has a skew to certain ingredients because we're asset light or we own more of certain businesses like the juice business vertically integrated in the US and [indiscernible] (43:09) in Europe than necessarily aluminum. And so, we do have an [indiscernible] (43:15) which is why we called out what we called out. I think the competitive advantage is not whether the company necessarily is asset light or not or has only certain commodities. Ultimately, we're a system with our bottlers where the pricing is taken by the bottler and then the company follows that along. I think the advantage is the global scale, the experience in managing through these environments and the ability to work with the supply ecosystem and create value for the retailers and the consumers.

Bonnie Herzog

Analyst, Goldman Sachs & Co. LLC



All right. That makes sense. Thank you.

Operator: Your next question is from the line of Kaumil Gajrawala with Credit Suisse.

Kaumil Gajrawala

Analyst, Credit Suisse Securities (USA) LLC



Hey, everybody. Good morning. Could I please follow-up on Bonnie's question as it relates to the incidence pricing model and maybe some of the new models that were put in in recent years? How does it work in this environment? Because the pricing is of course still taken by the bottlers, but I guess the relative price inflation, or the relative cost inflation is much higher at the bottler than it might be for yourselves. I understand that you take it as a system. But how does that work from an incidence pricing perspective? Does it still hold in that you are able to follow on whatever the bottler does in the marketplace? Or are there tweaks being made for what right now seems to be a bit of an abnormal situation?

James Quincey

Chairman & Chief Executive Officer, The Coca-Cola Co.



No, the incidence model works as the incidence model. And which, to be clear, is generally speaking the company's revenue on any particular brand or package is a percent of what the bottler is getting. It's not the same percent necessarily on every brand or even every package, but it is a percent. And then over time this has proven to be a great way of maintaining alignment and shared interest in driving value for the company and the bottlers' local management. So when a brand or a package or a channel or occasion grows, it's good for both the bottler and the company.

And if we decide to push on something that's more affordable, it delivers less for the bottler and the company. So the incidence has proven to be a tremendous vehicle of getting the franchise system to focus on creating value in the marketplace.

Over time in certain environments it puts – the rest of the cost structure puts a little more pressure on the bottler or a little more pressure on the company depending on what's going on. But we don't micro course correct the incidence for small problems or even potentially medium problems. We look at a holistic view of making sure the bottling system is structurally sound, has got the right capabilities, the right ownership and the right capacity to invest in the marketplace.

So if something completely pushes the thing off track, we're in a different situation. Otherwise we and the bottlers don't manage for the short term. We do manage the short term, but we think about it in the context of where are we going long term and manage through short-term effects.

Kaumil Gajrawala

Analyst, Credit Suisse Securities (USA) LLC



Thank you.

Operator: Your next question is from the line of Andrea Teixeira with JPMorgan.

Andrea Teixeira

Analyst, JPMorgan Securities LLC



Thank you. And good morning, everyone. James, I wanted to go back to your pricing commentary. If you can talk to your ability to continue to take pricing or if the actions you took so far, including the one you alluded to in North America in August, will suffice to mitigate the additional mid-single digit cost pressures in 2022. And how do you see the balance in between bringing back promotions to historical levels into 2022 for the at-home consumption? Thank you.

James Quincey

Chairman & Chief Executive Officer, The Coca-Cola Co.



Yeah, thanks for that. I mean obviously we're not at the stage of providing an outlook on pricing and promotion levels in 2022. We'll do that when we get to February. Certainly what we did in North America addressed the immediate 2021 issues in North America, as we did in other parts of the world, wherever it was in the world we would have addressed the cost issues and the earned brand pricing issues wherever we were.

Again, I think the important thing, the pricing approach is to earn the right to take the pricing for the brands. They earn that – the equity earns the right for pricing, and that's the combination of bearing in mind the cost inflation, the input cost inflation, the labor cost, the logistics cost, what we need to invest in marketing, what we need to invest in innovation, what we need to invest in execution and what we need to invest in coolers and routes to market. And that all goes in the equation of taking the pricing that we have earned to take. And that is the same balancing equation that we will look at for 2022.

Andrea Teixeira

Analyst, JPMorgan Securities LLC



Thank you.

James Quincey

Chairman & Chief Executive Officer, The Coca-Cola Co.



Sure.

Operator: Your next question is from the line of Carlos Laboy with HSBC.

Carlos Laboy

Analyst, HSBC Securities (USA), Inc.



Yes. Good morning, everyone. James, you mentioned strong US pricing several times. And in our Southwestern and US markets more recently, we also saw a major step-up in revenue management execution from pre-

pandemic levels. It's really sophisticated price pack structures that we're seeing. Can you give us a more broad-based North American assessment of how you see the market development capability of the US system improving over the next couple of years? And I guess what is the system going to be doing differently to keep driving this market development capability forward?

James Quincey*Chairman & Chief Executive Officer, The Coca-Cola Co.***A**

Yeah, sure. Well, thank you for those observations, Carlos, on the visits presumably in Texas or somewhere like that. As you well know, as a long [ph] connoisseur of (49:36) Latin America, we certainly have been trying to fuse together what the best of what the US system does with some imported thinking from Latin America on RGM and on the ground, up and down the street execution.

As we look forward into the US, clearly we're trying to bring the combination of more investment in the marketing of brands, more innovation targeted to the marketplace backed with the increasing use of RGM to be more sophisticated in the price and the mix opportunity. But also backed with ongoing improvements in the execution capability, not just in the larger stores or with the larger away-from-home partners, but also up and down the street with the smaller stores and really being within an arm's reach of desire, not just perhaps an arm's reach of job but within a click's reach of desire. And I think the [ph] the system, the execution (50:40) is continuing to back that as we go forward.

Carlos Laboy*Analyst, HSBC Securities (USA), Inc.***Q**

Thank you.

James Quincey*Chairman & Chief Executive Officer, The Coca-Cola Co.***A**

Sure.

Operator: Your next question is from the line of Robert Ottenstein with Evercore ISI.

Robert Ottenstein*Analyst, Evercore ISI***Q**

Yes. Thank you very much. First, just a quick point of clarification. If you could give the breakout of price mix in LatAm, how much was price mix and channel. And then my more substantive question. Some really great progress on the free cash flow side, significantly higher than your initial guidance. Can you talk about some of the drivers there? Are you where you need to be in terms of cash conversion at this point? And are these levels sustainable? Thank you.

James Quincey*Chairman & Chief Executive Officer, The Coca-Cola Co.***A**

Sure. I'll do the price mix, and then John can take the flowers and the laurels on doubling the free cash flow in the last few years. Price mix in Latin America, clearly there's a big component of rate in the third quarter, and part of that is driven by inflationary pricing in Argentina. But in the quarter, channel and package were both positive to mix, as was the timing of some of the deductions. And so, yes, it is rather an anomaly.

I think particularly in the case – I mean, it's generally true for the company that don't over rotate the quarterly pricing, particularly in emerging markets where there can be a tremendous amount of volatility because obviously we're quite far back in the supply chain. And so I would encourage looking at places like Latin America on a kind of a more multi-quarter basis given the volatility that one can get in terms of price fall mix given where we are in terms of what ships where. But generally speaking, there's a – it's mainly operational price and mix, and then there's a little piece that's inflation in Argentina. John?

John Murphy

Chief Financial Officer & Executive Vice President, The Coca-Cola Co.

A

Thanks, James. Yeah, on the free cash flow, we're clearly pleased with the progress we've made. Looking forward, a couple of observations. On our free cash flow conversion, our long-term algorithm has free cash flow conversion of 90% to 95% range. And I still believe that's the right level for us to be pitching at. This year is better than that, and due to some specific items through the year, our marketing accruals in 2021 were much higher than 2020 as the marketing spend returns to 2019 levels.

Our incentive compensation was down for obvious reasons in 2020 due to the pandemic impact. As I mentioned on the call earlier, we anticipate some headwinds in forex going into 2022. So taking all that into account, I would expect us to be still able to deliver against the range that we've outlined in the long-term algorithm.

Some of the drivers, Robert, in the last couple of years, we've made a lot of progress on working capital. We've talked about that in the past. We continue to do so. In a strange way, the one area that we are below where I would like to be is on inventory, but in a paradoxical way, that's been actually a good thing to have more buffer around the world. And so in the immediate short term, I kind of like it that way. But it's an area that we will continue to attack over time in a number of areas.

Operator: Your next question is from the line of Sean King with UBS.

Sean King

Analyst, UBS Securities LLC

Q

Hey, thanks for the question. I wonder if I can get your thoughts on some of the puts and takes to your bottling systems DSD capabilities in the context of some of the pressure points that other CPGs are having in keeping store shelves stocked, particularly around the coming holiday season. I mean, is it safe to say it maybe absorbing some higher costs but potential for share gains?

James Quincey

Chairman & Chief Executive Officer, The Coca-Cola Co.

A

Yeah. Clearly there's some pressure in the marketplace in terms of logistical capacity. And obviously with the holiday season tending to see demand go up, that's going to come into sharper focus as we go into the next few months. We are well set up. I think we are advantaged competitively. I would like to see us, as you say, make gains in not just the share of the visible inventory but in the share of the sell-out as well. We will see. Some of that is limited by some of the supply constraints. If we want to talk about the US, there is still – it's still tight on cans. It's still tight on hot-fill resin and so there is some limitations [ph] to what can be out there (56:16). But clearly as we sell lots of different brands in lots of different packages, we have the opportunity to make sure we can get the shelves full if not with absolutely everything we'd love to see on the shelves, at least the shelves will be full with the vast majority of the things we would like to see on the shelves.

And we can manage through it. I mean, if there's tremendous demand and shortage of supply, of course, one logically starts to wonder whether you need all the promotions that one can think of. And so there is a balancing of – if it costs slightly more to get stuff there because there are kind of shortages, then you don't need as much promotion. So I think there are a set of puts and takes here which will allow us, the system, to have a good holiday season.

Sean King

Analyst, UBS Securities LLC

Q

Great. Thank you.

James Quincey

Chairman & Chief Executive Officer, The Coca-Cola Co.

A

Sure.

Operator: Your next question is from the line of Chris Carey with Wells Fargo Securities.

Chris Carey

Analyst, Wells Fargo Securities LLC

Q

Hi. Good morning. I just wanted to follow up on this outlook for mid single-digit inflation going into next year. I mean, conceptually spot prices are decidedly higher than mid single-digits. Perhaps I'm reading that dynamic wrong. But if I'm not, is this simply a function of your global scale, your ability to source and massive [ph] iteration (57:54) prevailing? You just noted that inventory has been [indiscernible] (57:59) free cash flow, but that's actually been a buffer which has helped you actually in this tight inventory position. So just, I guess, any perspective around that would be helpful because this is a dynamic we've been seeing where spot is actually quite a bit worse than how companies are looking at the go-forward. And I'm just curious on perhaps why that is the case and why you might stand out in this regard? Thanks so much.

James Quincey

Chairman & Chief Executive Officer, The Coca-Cola Co.

A

Yeah. Two things to bear in mind. And let me start with the company and talk about the total system. We the company obviously skew, as I mentioned earlier, in terms of the commodities that flow through our P&L most directly. And bear in mind, the biggest commodity that flows through the company's P&L is actually juice, the cost of buying juice, whose spot price has not shot up. It was not projected to shoot up as much next year as this year. It has obviously increased in 2021 over 2020, but it is looking more in the range that we've talked about going into 2022. So from the company's perspective, our biggest commodity is not – that the spot price of it for next year is not wildly projected to be out of line with what we're talking about in terms of the increases.

And then obviously, we buy a whole set of other things which are expected to go up. So I do want to also encourage you to remember that we don't buy heavily on spot. That is not our objective. As I talked earlier, given our scale in most commodities, especially as a system, we look to buy on a long-term basis, not just hedging on a long-term basis or a multi-quarter basis, but buying with partners and making commitments on a long-term basis too. And so we don't go up and down with the stock market on a day-to-day basis. And that means that the system also has the ability to lock in while still inflationary in 2022, whether we're talking about PET or metals or sugars or corn syrup that they're all going up in 2022, but it's not that the sky is falling.

Chris Carey

Analyst, Wells Fargo Securities LLC

Okay. Thanks so much.

James Quincey

Chairman & Chief Executive Officer, The Coca-Cola Co.

Sure.

Operator: Your next question or final question is from the line of Kevin Grundy with Jefferies.

Kevin Grundy

Analyst, Jefferies LLC

Great. Thanks. Good morning, everyone. And congratulations on further progress in the quarter. James, I wanted to pivot to the energy drink category and your broader strategy there as performance energy brands have accelerated industry growth and taken share from brands like Monster. So clearly your stake in Monster underpins the company's broader strategy, though you've also obviously rolled out Coke Energy, AHA with caffeine. You're rolling out RTD coffees in certain markets. So I'd like to get your updated thoughts on, one, how the category is evolving and, two, your overall level of satisfaction with your energy drink strategy particularly in some of these niche and upcoming brands that are gaining market share from brands like Monster? Thank you.

James Quincey

Chairman & Chief Executive Officer, The Coca-Cola Co.

Yeah, sure. Let me distinguish clearly between the energy drink category and the energy or recharge need state as you mentioned a series of other brands as well. As it relates to the energy drink category, obviously we have a very successful partnership with Monster that has created tremendous value for us, for the bottlers, and in particular for Monster. And I think that's driven lots of it, yes, there have been in the US some recent competitive entries which seem to be both expanding the category and taking some share. Obviously, you see in their numbers, I know they haven't announced it this quarter but at least for the numbers they've announced for the first half so far this year, you can see they continued to grow strongly this year on top of growing last year. So there's a lot of success and I'm sure they'll talk about on their call how they're responding to marketplace dynamics and obviously with the system look forward to continuing to drive success with that partnership.

As it relates to the broader energy need state or recharge need state of consumers, clearly that's growing. It has been growing pre-COVID, and it's still growing, whether that be as you say ready-to-drink coffees or some of the caffeinated waters, we see a lot of focus and opportunity for growth there. Cost of ready-to-drink has done – cost of coffee ready-to-drink has done well where we've launched it. AHA has done well when we launched in China. And certainly there's kind of caffeine being introduced with a number of different beverages here in the US. And so we do see ultimately the kind of recharge need state whether that's satisfied with an energy drink or a Coke Classic or AHA with caffeine or a Fairlife Chocolate milkshake, that has been a long-term driver of growth in the beverage industry and we expect it to remain so.

Kevin Grundy

Analyst, Jefferies LLC

Very good. Thank you.

A

James Quincey

Chairman & Chief Executive Officer, The Coca-Cola Co.

You're welcome. Okay. I think that was the last question.

James Quincey

Chairman & Chief Executive Officer, The Coca-Cola Co.

So to summarize, we're confident that as the world begins to move beyond the pandemic, we'll deliver against our long-term growth model, consistently and sustainably over time. And from putting our new marketing model into action, to shaping a strong and enduring innovation pipeline, from our digital initiatives, to our important sustainability agenda, we are working in alignment with our bottling partners, with the power of our people and we are poised to drive growth at scale for the entire system for years to come. So thank you for your interest, your investment in our company and for joining us this morning. Thank you.

Operator: Ladies and gentlemen, this concludes today's conference call. Thank you for participating. You may now disconnect.

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