



The Coca Cola Company | Deutsche Bank | 2022 dbAccess Global Consumer Conference | June 16, 2022

Stephen Powers:

Okay, welcome back. For our next session, I'm very happy to welcome back The Coca-Cola company to the conference. Chief Financial Officer, John Murphy. I see there's a typo on the slide, so I apologize for that. James is not aware.

John Murphy:

James would not be happy.

Stephen Powers:

As well as "Manolo" Arroyo, the chief marketing officer for the company. We're going to use the session for Q & A. John and Manolo, thanks for being here. We'll just get right into it. I guess, just to start, even before the volatility we've been talking about for three days around the pandemic, around inflation, Russia, Ukraine, and other things, Coke, as a company, as a system, had embarked on a journey of transformation preceding all of that, and I guess, first question is just, how would you assess the journey that you've been on and score the journey that you've been on so far and what are the biggest opportunities that you see still ahead?

John Murphy:

Good. Well, see, thanks for having us and thank you everybody for joining us. Yeah. It's hard to believe it's three years ago since we were together on this stage, and so, a lot has happened, and I think the journey that you refer to, we had started maybe the year before then year, year and a half before then. It's one that really has been designed around the consumer to become a total beverage company, and to do so in a systematic fashion, not overnight, but over time. I think the years 2020 and '21 have had... the two words I think of, they were provocateurs and they were catalysts, because I think that period, particularly the period in 2020, the second half of 2020, I think it provoked all of us to take a step back and to really challenge ourselves as to what is required to sustain growth at the top end of our algorithm, which is what we aspire to do.

John Murphy:

We also were given what I think, as I look back, a window to make changes that would probably have been harder to make in more normal times. What we have seen come out of that is, I think, with a stronger portfolio of brands, Manolo can talk more about that in the course of the conversation. We have really focused on improving the quality of our marketing and innovation as a company across all of our categories, not just be good on occasions. We have, and I've seen a number of our colleagues from

around the world in the room, I think we have come closer as a franchise system end-to-end to deliver more sustained performance in the marketplace, regardless of the conditions. Inside of The Coca-Cola Company, we have started, I wouldn't say a [inaudible 00:03:39] finished, a pretty radical departure from how we historically were organized in more hierarchical, more siloed, to one that's a lot more, as we call, networked, a lot more about having the right people doing the right things at the right time and the right places, is not much more complicated than that.

John Murphy:

But those are all elements where, I think, we have seen tremendous progress, and yet the journey is far from complete. Last part of your question, worthy opportunities ahead. I think our theme for this year internally is all around executing for growth. I think of execution across all elements of, "What does it take to be a better company, a stronger system, and be in a position to deliver on a strategy?" I think is fairly straightforward with the executional components, whether it's on the marketing front, whether it's on the supply chain front, whether it's on the people management front. There's still a lot of runway ahead to get those to what we call Olympian levels of performance.

Stephen Powers:

Olympian. 'Asynchronous' has been a word that you've used, James has used quite a bit describing the nature of recovery from the early stages of the pandemic. Now we've got additional volatility. I guess, how would you describe operating conditions today in that context, and what gives you confidence that through that volatility you can consistently deliver at the top end of that long term growth algorithm?

John Murphy:

Unfortunately, I would say that the world has still got plenty of application. It's a word I [inaudible 00:05:33] used prior to July of 2020, and yet we do see different exits from COVID around the world. We see some parts of the world falling back into it. In China, been our typical example, and we've seen conditions in Europe and in other parts of the world actually been less clear than I thought they would've been when we kicked off 2022, so I think the word 'asynchronous' is still very relevant and one that we will unfortunately continue to use to summarize what I'd call a global portfolio that's got many, many moving parts inside of it. What gives us, I think, the confidence that we are on a good path to deliver sustained performance over time is, first and foremost, the industry that we operate in. If you go back over the last 30 years, and we've done so to reassure ourselves that the trends are as consistent as we feel they are, the industry's growth patterns have been quite predictable.

John Murphy:

Yes, you have the occasional anomalous period where you're either outside of the range or below the range of 3 to 5%, so it's an industry that has got quite a predictable pattern of growth, and we expect that to continue. Now, inside of the industry, categories grow at different rates, but overall, part of the rationale for wanting to be a total beverage player is to be able to participate in the various slipstreams that are available inside the industry at a given time, so industry growth number one. And then number two, what I've talked about, the journey that we're all on is a journey to be better. We're not here to just play, we're here to win, and we want to win both absolutely and relatively, in the marketplace. I think the kind of portfolio that we have, and we're developing and nurturing, the step up in marketing and innovation, the quality of collaboration that's happening with our partners in the marketplace, the revenue growth management tools that we've talked about.

John Murphy:

They're all designed to give us the edge that we think we need in order to win absolutely and relatively in the marketplace. If you believe all of that, which I do, then the high end of the algorithm is, I think, achievable.

Stephen Powers:

Achievable. Manolo, as you look through the current dynamic operating environment, what are the evolving consumer trends that you're able to distill, number one, and then what does The Coca-Cola Company system need to do to capitalize on those trends? What role does marketing play and how you measure the effectiveness of that marketing?

Manuel Arroyo:

Okay, thank you. We are, as John mentioned, a company that all starts on the consumer, and when we look into trends globally, we obviously leverage, basically, data and analytics. There are few trends that unquestionably have been for some time playing out, and during the pandemic, actually, most of them have been accelerating. Health and wellness is one of them. ESG consciousness is another one. Convenience has even accelerated further during the pandemic. There are a few others. For example, it's a busy world, busy and stressful world. People need more and more functionality, and that is what is behind of the growth acceleration of coffees or energy drinks, or even colas, for that matter. So, the way we think about approaching and leveraging those trends, it's basically in the new marketing model. It's leveraging a massive shift that is going

Manuel Arroyo:

... going on with the consumer, and that shift is coming from an old marketing world of TV-centric. Consumers around the world, regardless of the age, are moving massively outside of traditional TV consumption, going into subscription models, consuming digital. And in that context, we realized that it's not anymore about just putting an ad, a TV on television and just expecting sales growth. So we're moving to a world of experiences and experiences are for us a kind of a perfect blend between passion points that people go who are in love, music, gaming, sports with consumption occasions. And I think this is a critical component of a marketing model of the Coca-Cola Company that you can expect in the next decade.

Manuel Arroyo:

Consumption occasions are basically about explaining someone that doesn't drink our portfolio today, when, where, and why they should consider one of our brands in a unique way. How do we measure that? I would say two major metrics. First one is consumer based, the consumer base for us as a metric, which is weekly plus meaning from every 50 beverage occasions that a normal human has in any given week, the moment you every week, at least one of those 50 repetitively, you do that, you're consuming one of our brands, we consider you as one of our members of our consumer base. To give you a perspective, Coke, Coca-Cola consumer base is slightly below half billion consumers in a planet of 7.7. So still, the growth potential is just phenomenal.

Manuel Arroyo:

And the second metric critical in marketing is around the effectiveness of our marketing. And we look into particularly how much profit are we driving their invested dollar in marketing. Last year, that metric grew 7%. The last metric that we've been traditionally working on is the level of the equity of our

brands. Equity is very important because it allow us to... It's what we define as earning a right to take pricing.

Manuel Arroyo:

So moving forward, you will see how we move more into ensuring that we first drive our consumer base, but also increase our equity at least in line or more than inflation so we earn our right to our bottling partners to take pricing consistently moving forward in a balanced way.

Stephen Powers:

And is the burden on marketing efficacy even higher in this environment where you're asking consumers to pay more year over year, whether it's through price increases or revenue growth management?

Manuel Arroyo:

I would prefer to think I was born with the burden-

Stephen Powers:

Okay.

Manuel Arroyo:

Regardless of the macroeconomic condition.

Stephen Powers:

Okay.

Manuel Arroyo:

So I see the role of marketing one that we have to drive every single year, both effectiveness and efficiency, and both are critical sides of the same equation. The opportunities for efficiency in our marketing, I fundamentally believe, are endless and effectiveness, even more. So part of the algorithm or in the discussion internally with our 2,000 marketeers is well, before you come asking for more funds, we're ready to invest and we love to invest more and more in marketing, that's we got to make sure first that the base of our marketing investments, which is very substantial, is as effective and as efficient as it should be.

Stephen Powers:

Okay. Great. John, maybe a little bit more general context of inflation from your perspective. I guess how are current costs and I'd add FX pressures trending for the company and what are you seeing today in terms of elasticity? What are you expecting? And I'm sure it's not a point expectation, it's a range of scenarios, but just how you're thinking about consumer demand in that respect today and how it may vary across the world.

John Murphy:

Sure. So let's maybe anchor back to our Q1 call. We talked about the commodity environment for the company and there's really been no significant change. There's nothing really too much to talk about there. I think the inflationary pressures in non-commodity inputs in a number of important markets are there [inaudible 00:15:15] I think everybody's talking about them. I think in the case of Manolo's world,

there's no significant area that's immune from increase pressures, marketing expenditures, operating costs, et cetera. So I think like other companies who you've spoken to during the week, I think those pressures are real and they're going to be with us for a while. There's no question about that. How it all manifests, particularly towards the end of the year and into '23, I think we're all watching very closely.

John Murphy:

Thus far, the consumer has been pretty resilient. And I think one of the reasons for that is that, first of all, they have had more money coming out of the pandemic to spend. Number two, the lack of alternative ways to spend it, i.e., travel, movement around has honed them in on affordable luxuries at home. We're seeing in some markets the durable sectors, which is very typical in inflationary periods for the durable sector to be the first one to show signs of pressure. And I don't think you need to be a genius to sort of figure out that the overall cost of the household basket is rising, particularly in the United States and in Western Europe. I don't think Asia has seen the same levels of pressure yet. And in the developing world, I think they're more used to it. They're more used to, and so there's more of an automatic adjustment to it. So I expect that to continue.

John Murphy:

We've talked a lot about the ways to mitigate that through intelligent revenue growth management, using pricing, but using it intelligently. And I think the system is demonstrating that the capabilities that are being built around the world over the last number of years are actually paying off at the moment in the way that we are deploying it.

John Murphy:

What the outlook is towards the end of the year and into next year, I think, is too early to call. I think it will be asynchronous as well because that's the way the world is evolving. But for sure, it's going to be a key topic. And I think on our July call, we'll give a more detailed update as to how we're seeing [inaudible 00:18:08] through the rest of the year.

Stephen Powers:

Okay, great. You mentioned working within the system. Is being franchised at a time like this an advantage, a disadvantage, agnostic?

John Murphy:

Well, I think we would be somewhat biased in our views of the franchise model. We think it's a great model to have in good times and in tough times, but like any model, it's all about how you implement and execute and lead it. I think the quality of leadership that we have today in our system is as strong as I've ever seen it.

John Murphy:

We operate not just a franchise model. We operate in an ecosystem. Some of the suppliers that we have been working with around the world over the last three or four years have been extraordinary in the way that they've come to the table to help us all mitigate against tremendous pressures. The customer relationships that we have around the world are extraordinary. We have over 25 million customers around the world and the way that the systems has engaged and has been reciprocated has been powerful.

John Murphy:

So I think the franchise model is part of a broader ecosystem. And that ecosystem, I think, has emerged very strong from the last couple of years. And I expect it to be a big advantage for us going forward.

Stephen Powers:

Okay. Manolo, we spoke of marketing effectiveness earlier and you talked about how you'd love to spend more. I'm sure John would actually agree, assuming the ROI is there. Is there greater pressure in an inflationary environment like this on marketing efficiency to get those incremental dollars?

Stephen Powers:

How does your organization, and how do you kind of balance those top and bottom line considerations, the desire for more marketing versus the bottom line implications?

Manuel Arroyo:

Well, against the advice of asking for more, there's always the pleasure of saying no. But as a principal, a marketer is always going to ask for more funding. But the way we're seeing moving forward is we definitely want to invest more, but on the basis of really efficient and effective investment. One of the key things that we are putting in place is a very structural capability called experimentation, which is allowing us specifically on marketing effectiveness. And what this is about is leveraging experimentation to become a learning organization, leveraging experimentation as a superpower. And that specifically is about having anywhere between 200 to 400, depending on the year, experiments distributed across the wall that measure specifically dollar investment to transactions and impact at the customer, at the point of sale.

Manuel Arroyo:

Today, seven of the nine operating units already have, as we speak today, experiments in the market. Some of the learnings are mind blowing of the amount of extra revenue growth that you can drive with exactly the same dollars. Let me give you an example. Buying media in the US on a demographic basis, versus for a Sprite, versus buying on an attitudinal standpoint. So instead of targeting everyone between a certain age, I'm going to talk to only three tribes in the US. Three consumer tribes. From an attitude perspective, it can drive you six to seven points incremental NSR growth for the same dollars. And that's just one of those 200 experiments. That is a fundamental component of our equation moving forward.

Manuel Arroyo:

The second one in this new context... Again, occasions are going to be critical to explain or to move humans that are not part of our consumer base to become part of our consumer base. And that's important because we were really good in the past explaining why we were either functional or emotional standpoint, but we were not telling them when and where. And it is also very critical in our case because if there's a language that unites us with our bottling system, our occasions... Occasions are very easily translatable into channel execution strategies. And a lot of times in the past in marketing, we were not getting that far as we should to be able to bring the consumer into our portfolio.

Manuel Arroyo:

Those two components in this new environment are going to be absolutely critical to have the flexibility and the muscle to adapt to that synchronous evolution that we're going to see forward.

Stephen Powers:

So the idea is experiment, scale up the ones that work.

Manuel Arroyo:

Correct.

Stephen Powers:

Fail fast and cheaply, hopefully.

Manuel Arroyo:

Yeah.

Stephen Powers:

On the ones that don't.

Manuel Arroyo:

And the way we do it, for example, one experiment in one operating unit, let's say Europe. As part of the multifunctional team, you have the experiment leader of North America and Japan for the next quarter. So next quarter, another two of the nine operating units. In the next two, North America and Japan, you have two, one each, of two other. So in nine months, you've covered seven of the nine operating units. The moment you see a pattern after four to six months, then you would just deploy that globally through our partnership. Particularly, for example, on media buying [inaudible 00:24:21]. So it's a very different way. In the past, we did some of this, but we were not good at scaling this quickly and rapidly across the system.

Stephen Powers:

And how would you assess marketing works, assuming the marketing's effective but the products also sort of resonates with the consumer itself. So how would you assess, Manolo, the current innovation pipeline and recent innovation launches of the company? Not just in terms of product formulations that have resonated with consumers, but also in terms of being able to deliver on consumer demands around affordability, sustainability, and so on.

Manuel Arroyo:

We have as part of the new redesign of the model, of the company, with revamp upside down our capabilities in innovation. Today, we look into three major buckets. One is consumer desirability, financial attractiveness, and technical supply chain visibility. As we stand today, we have a portfolio for 2022 that is composed of around 1500 different innovations. And that includes product packaging and equipment. The bigger bets represent around 65% of them. We have segmented all of those innovations. It's segment of them, we call it epic projects, big projects that have the potential to attract no less than a hundred million consumers around the world, and generate in less than three years more than a certain benchmark of NSR and gross profit.

Manuel Arroyo:

And today, our pipeline basically is contributing to around one third of our incremental gross profit. Last year and this year will be the case. As of today, our pipeline for '23 and '24, it's around 50% is stronger than what was our pipeline at the same time last year. So really, really excited. John has been particularly hitting very hard on the role of innovation. Because our prior innovation, we have too many failures. We had a wonderful success rate versus the industry, but that success rate was 3%. The problem was not... 3% was not good, it's that the industry just that 1%. So we see a significant room of improvement to take that up.

Manuel Arroyo:

We have great examples, not only from a product standpoint. On a product level, we work on scale innovation. Example of that would be Coke Zero, [inaudible 00:27:16] or [inaudible 00:27:17], or what we're doing in fairlife. And then some experimentation. So Coca-Cola creations. This one is a clear example. And we're seeing phenomenal success. This one, for example, it was the first month, 60% more than vanilla orange in 2020. And it's not a coincidence. This revamp of the process is clearly helping us to understand what are the drivers and what we were not doing that well in the past. When you move to packaging, there are big bets on sustainability and affordability. Examples of that, affordability is the ASSP PET technology that allow us to hit a 15 rupee price point, affordable entry price point in India. Very critical. We're selling everything we produce. Every new line that comes into place, it also goes immediately. And that's a good example.

Manuel Arroyo:

Or I'm very excited, for example, of the labelless packaging development in Japan. They have there the habit of... As you may know, in Japan, consumers are required to separate the label out of the bottle and recycle those two separately. We're selling that only through Amazon and eCommerce at that very significant premium. And basically also working really well, moving now into China, Hong Kong, and a few other countries. A lot of interest on that front. Or in Germany, leveraging the habit of returnability. This is more a premium play. We just launch 330ML returnable glass bottle at a premium price. And one liter RGB, returnable glass bottle, which is a much better and much more profitable, much higher margins that are two liter [inaudible 00:29:20], also in Germany. So those are a few of them, many examples that we have across the system.

Stephen Powers:

That's great. We spoke earlier to Brown-Forman about the Jack Daniels with Coca-Cola launch. That's a launch now. That builds on... We've got Topo Chico, Simply, Fresca Mixed. There's a bunch. We've got now got a full slew of portfolio, including an alcohol launch under your flagship brand. Does that mean that we as investors should no longer consider a foray into alcoholic beverages as a experiment for the Coca-Cola company? And now this is

Stephen Powers:

Becoming increasingly part of the company strategy.

Manuel Arroyo:

When you look into consumer trends, this is a very interesting space for us, as consumers are clearly moving into that space. Which is what we call it flavor alcohol beverages, pretty much in the space

between beers and soft drinks. We are still experimenting with the three different major segments within that, which are basically hard seltzers, that's top of Chico.

Stephen Powers:

Yep.

Manuel Arroyo:

Hard alternatives. And that's where you have the example of Simply, and then premix cocktails, which we were already actually there since last year with Strips. Premixed cocktails in Brazil, doing actually very, very well. Surprisingly well, I was a bit more skeptical. The good thing is that when you're wrong and the team is right, the network is working and this is obviously a very exciting one because it involves our most iconic brand.

Manuel Arroyo:

We are leveraging on the top number one bar call out there. There is definitely a lot of excitement. It's a global deal. We're only starting in Mexico this year, and then more markets to come next year. I'm personally very excited for multiple reasons. We're not going to see the traditional TV advertising of Coca Cola, is going to be very much digital influencers is tapping a lot into at home consumption occasions, not necessarily away from home that much. And specifically from a product not only the iconic Jack and Coke, but you're also going to have a zero sugar version that has 100 calories. So, as someone that likes, not a lot but once in a while, a beer and I also like whiskey and Coke. When I look those 100 calories, obviously coming from the whiskey, it's a pretty good alternative because I got to take care of my calories in and versus a beer, it's a very, very interesting proposition. So we see a lot of potential still learning. We're still going to iterate some of the components. The packaging graphics are strong.

Stephen Powers:

It's very cool. The can's cool.

Manuel Arroyo:

And the repeat rate of the liquid of the formulation. Once you taste, it is just phenomenal is one of our best products, in my mind, ever in the history of the company.

Stephen Powers:

Great. We have about five minutes left. John. I want to hit on cap allocation, which I think you've been very clear on really, since you got into the role. But maybe a few words on how you think about capital allocation priorities day to day, how events of the last six months have challenged any of the going and thinking if they have, maybe inclusive the decision this week to delay the CCBA IPO and just how you'd frame any constraints around more discretionary capital allocation? Which I think investors tend to think about as share purchases or M&A, but I'd also add just discretionary reinvestment back in organic business.

John Murphy:

Yeah. It's a hugely important topic, as everybody in the room, I think, appreciates. Our framework is very consistent. And I think to your question, the devil is in the details. The challenge of not just allocating

capital in an effective way across the portfolio of options, whether it's investing in the business, supporting the dividend, looking at inorganic opportunities, share repurchase, and the one that often gets left to one side is making sure that you do all of that with an optimal capital structure. So I think we're very clear on the framework, we have a point of view as to the allocation. But going back to some of the comments that Manolo was making, it's one thing to put money into an area. It's another thing to do it well, and to continue to drive greater returns from it, so.

John Murphy:

I think to the point on discretionary investments, all is interested in discretionary investments to drive the core business. I think in the environment that we're in at the moment, and the data that we have been in, I think one of the big takeaways from the last couple of years is that capital efficiency needs to be measured. Not measured in the sense of... But it needs to be a measured process because you can become almost too efficient and not leave yourself a little bit of slack for the days that you need that slack to help you manage through shortages or shots. And so I think on the discretionary front, one of the things we are looking at as we go into the rest of this year and even into next year is what does it take to become even more resilient?

John Murphy:

What does it take to feel confident about managing whatever future comes at us? I've been in the prediction game right now is a kind of a... The problems are pretty low given what we've seen in the last couple of years, but I think getting into a different game and that is getting ready for whatever gets thrown at you and being as best prepared as you can. I think that's challenging our system, not just the company, but our bottling partners too, to think maybe a little bit differently about not only how we invest, but what we invest in. And so I think that's a, ultimately. Can be an opportunity for us.

Stephen Powers:

Okay. On the CCBA decision, is there a way to frame any milestones or gates that you would go through to reengage on that?

John Murphy:

Yeah, I think the overall way to look at it is that the decision to postpone, I don't think shocked to many people given what's happening in the capital markets. I think as soon as, and as long as we see some degree of normalcy return... One man's definition might be a little bit different than others, but I think there'll be some variables to that formula of normalcy that we continue to look at. And the overall strategy around our bottling investments and over time continuing to have partners in those franchises come in as investors and run them has not changed. That continues to run its course.

Stephen Powers:

Okay. We're just about out of time. I've been asking just about everybody the same question at the end. When we reconvene here in a year, not three years hopefully, a year, what are the one or two things you want to be able to say you delivered on over the next 12 months?

John Murphy:

For me, it goes back to what I said at the outset. It's about execution. The strategy is clear. The journey ahead to become a total beverage company, total beverage system is clear, we're relying on it. But to me, raising the bar in every important aspect of how we do business is the ultimate test. And I'd like to,

first of all, I'd like to be back here next year, I think Manolo would too. And, but I'd like to be back and be able to talk about a raised bar for the Coco Cola system.

Stephen Powers:

Great, John. Manolo, if you want to add, go ahead.

Manuel Arroyo:

I mean, very simple. As I mentioned, the role of marketing is about bringing more consumers into the portfolio and spending the marketing funding in a much more effective way. Then all of that wrapped around at the end of the day, we are a marketing company. So ensuring that the magic of our marketing really drives all the energy, all the passion, all the drive to execute the whole system. And that's maybe why our current big umbrella is about real magic.

Stephen Powers:

Very nice. John, Manolo, thank you very much. Thank you both for joining us.

John Murphy:

Thank you.

Manuel Arroyo:

Thank you.