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Epochal Deal: Coke Is Buying CCE's North American Business. \$13 Bil Deal. Kent Expresses Confidence in Management. Sees Future Role for 'Partnerships.'

Coca-Cola Co and CCE have reached agreement on a deal which will dramatically change the North American Coke system. Coca-Cola Co is buying from CCE its North American business. CCE will get from Coke its bottling businesses in Sweden and Norway. CCE is also getting the right to acquire in the future Coke's bottling business in Germany. Coke is contributing back to CCE the 34% equity stake it owns in CCE and will be assuming some CCE debt. Total deal value about \$13 bil, according to several sources. As a result, assuming it completes the deal with CCE, Coke will own about 75% of its North American system, measured by CSD volume. CCE will continue as a public company, but without Coke ownership. Its territories will cover its current European footprint: U.K., France, Belgium, Luxembourg, Monaco and the Netherlands; plus Sweden, Norway and possibly Germany in the future. In 2009, North America accounted for 73% of CCE's total bottle/can volume, and Europe accounted for 27%. So CCE will start its new incarnation as a much smaller company. Source says over time CCE may expand its footprint in Europe, if other bottlers want to sell territory. **Deal long in works.** Coke CEO Muhtar Kent told **BD** that Coke and CCE have been working for more than a year on creating this new structure.

Coke and CCE Deal Details. Coke says \$13 bil deal is "substantially cashless." In exchange for getting CCE's North American business: 1) Coke gives up its 34% equity interest in CCE, valued at \$3.4 bil. 2) Coke assumes \$8.88 bil of CCE debt. 3) CCE gets Coke's Norway and Sweden bottling operations, valued at \$822 mil and the right to acquire Coke's 83% equity stake in its German bottling business 18 to 36 months after the closing. **Plus.** CCE shareholders, in exchange for their existing shares of CCE, will get one share of new CCE stock plus \$10 cash per share.

Management; headquarters, etc. CCE will continue to be headquartered in Atlanta with a European headquarters in London, according to sources. CCE will continue as a NY Stock Exchange-listed company. John Brock will continue as CEO; Bill Douglas as CFO; and Hubert Patricot, who runs Europe, will continue in that post. Steve Cahillane, who runs CCE North America, was not mentioned in the Coke-CCE press release, and sources say he may have continuing role in North American Operations. Kent, in interview, expressed confidence in Cahillane, Coke North America head Sandy Douglas and the entire North America management group.

PepsiCo Comparison. Coke announced this deal on what is likely the day before PepsiCo completes its purchases of Pepsi Bottling Group and PepsiAmericas. Assuming the Coke-CCE deal completes, the Coke and Pepsi bottling systems will look very similar in North America. PBG and PAS together account for about 75% of PepsiCo North American CSD volume. CCE accounts for about 75.6% of Coke's North American CSD volume. Kent has said he is committed to the franchise system (**BD** 1/15/2010), and in fact 70% of Coke's global volume will still be handled by franchised bottlers. But, most of its North American volume won't be, after this deal gets done. Some bottlers and others had believed that Coke would have had challenges in competing with a Pepsi system largely owned by the franchise company. **Ahead.** Assuming the Coke-CCE deal gets done, a large part of the North American Coke bottling business will be owned by Coca-Cola Co. Some sources wonder what will happen down the road with the North American business Coke is acquiring. Will it keep it long term? Re-franchise it? Or perhaps sell it, possibly to Coke Femsa? Some have recently speculated on a move by Coke Femsa into North America (**BD** 2/12/2010).

Is 75% a Solution? Sources expect Pepsi down the road, having bought its two large bottlers, to make some route-to-market changes, including possible warehouse delivery of some products to some retailers. Some thought it would be more difficult for Coke to do this, with a system mostly made up of franchised

bottlers. Now, Coke will, like Pepsi, own about 75% of its system. However, for both Pepsi and Coke, achieving changes in routes to market with national accounts will be an issue, as long as significant amounts of system volume are handled by bottlers not owned by the franchise companies. Multiple sources believe that PepsiCo will buy more bottlers to get its system ownership up to around 90%. It would stand to reason that Coke may need to do the same.

Dr Pepper Snapple. CCE is the largest Dr Pepper bottler and the #2 bottler of all Dr Pepper Snapple CSD products combined. CCE handles 27% of Dr Pepper volume and 14.3% of DPS volume. PepsiCo is paying DPS \$900 mil to keep the Dr Pepper and other DPS brands that were handled by PBG and PAS. The PBG/PAS contracts had so-called "change-in-control" provisions, requiring DPS's consent to the transfer to PepsiCo. If CCE's contracts have similar provisions -- and two sources suggest they do -- Coke will have to negotiate with DPS, as did PepsiCo, and possibly pay a large amount to DPS should it wish to keep Dr Pepper and the DPS brands.

Executive comments. Kent stressed that Coke is "not acquiring CCE, rather we are acquiring their North American assets." He says CCE, under the leadership of Brock, "remains one of our key bottling partners with world class management." Adds: "This deal is different from any other deal of its kind. The heads of the two businesses are totally aligned." Plus, "we are strengthening a franchise system in one of the most important geographies of the world, Europe." Also: "This deal will evolve with a final picture where there will be a clear, meaningful role for partners in North America (and) will facilitate innovation." Brock says the CCE management team and board "strongly support this move." Adds, "we think from a strategic standpoint that this is the right thing to do for all major stakeholders. It is the moment in time to have this paradigm shift. It will create value for all our stakeholders."

Interview. BD asks Kent: Why Do Deal? "Our franchise system in the U.S. has not changed since 1986. The customer, the landscape and the consumer have evolved. We are still an ardent believer in our franchise system, but it needs to evolve. This is a logical evolution to ensure our ability to keep winning in the largest profit pool in the world, which is North American non-alcoholic beverages ... Coca-Cola Co will work closely with its bottling partners to create an evolved franchise structure for the unique needs of the North American market. In Europe, CCE is further strengthening our franchise system." **Motivated by PepsiCo Deal?** "CCE and and Coke have been working for more than a year on ensuring that we can create such a structure."

Will Coke Keep North America Bottling Business Long-Term? "The North American business is very different from our international businesses ... We have an integrated fountain business run separately. We have an integrated juice business run separately. Out of the 117 production locations in the U.S., we operate and own more than half of them. We have a very big asset base in the U.S. already. And therefore it makes sense for us to fuse all of our businesses together under one roof and generate synergies ... We have a number of stages that we are going to go through before we reach the end-game. The end-game that we see in the U.S., however, will have a meaningful role for partnerships as we move forward. It will be a more efficient system that we will create."

Need to Buy More bottlers? "When this transaction is complete, we'll have more than 90% of volume in our control (including DSD system plus fountain, warehouse, etc.). That will enable us to start really reaping the operational synergies and efficiencies." **More Bottler Acquisitions Ahead?** "I would not want to comment on that. All I can tell you is very clearly that over the past months we've had productive discussions with all our North American bottlers about the absolute need to evolve in order to better serve our customer and consumers."

Management? "I'm going to come back in April to talk in more detail about the integration team and efforts as well as the management thereof. We have tremendous faith in the Coca-Cola Co North American management and in the CCE management across North America and overall ... CCE has first-class management, first-class capability and first-class customer service ... I have great faith and respect for Steve Cahillane and for Sandy Douglas, and we will talk in more detail about integration and management."

Want to keep Dr Pepper? "It would not be appropriate for me to comment on the terms of CCE's current relationship with Dr Pepper Snapple, however we envision an on-going business relationship with cross-franchise companies like DPS, with which CCE has had a mutually benefit relationship."

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