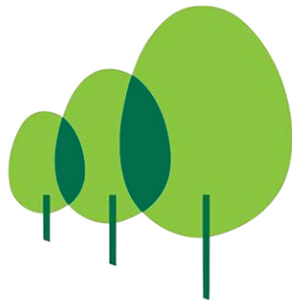


# Scoring **Coca-Cola's** 2015 Proxy

The “Big Grab” was halted, but urgent issues remain to be addressed



**WINTERGREEN**  
ADVISERS

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A year ago, Wintergreen brought attention to what we saw as serious pay and governance problems at The Coca-Cola Company, beginning with a proposed equity compensation plan we called “Coke’s Big Grab” for its potential for whopping payouts to management.

Many Coca-Cola shareholders came to share our view, and Coca-Cola took some positive steps. Yet despite this progress, a review of Coca-Cola’s 2015 Proxy Statement suggests improvement has been slow. To us, revitalizing this storied American brand requires more accountability, stronger leadership and a greater sense of urgency.

The board continues to give Muhtar Kent and his team what we view as excessive rewards, and we question whether many directors are able to vigorously act for all shareholders. Coca-Cola’s results remain far short of our expectations, and performance metrics that are not met by executives appear to be excluded from compensation decisions. We think the board and management lack a sense of urgency to address Coca-Cola’s problems and increase shareholder value.

Wintergreen plans to vote against Coca-Cola’s carryover directors because of their unanimous support for the controversial 2014 Equity Plan. The current board has not exhibited the type of leadership and independence that we believe Coca-Cola requires to get its business back on the path to profitable growth. We also believe the new director candidates are not likely to provide independent thought given their overlapping connections with Coca-Cola and other directors; we will therefore be voting against them as well.

## One Year Later: Progress, but More Change is Needed

There has been progress on the issues Wintergreen identified a year ago, but we think Coca-Cola's management and board must do more to restore investor confidence, hold management accountable and restore the company's profit growth. If they cannot, they should be replaced.

Over the past year, Wintergreen brought attention to five issues where progress was made:

### Executive Compensation

A year ago, Wintergreen opposed Coca-Cola's proposed 2014 Equity Plan because we believed it was a bad deal for shareholders. We called it "Coke's Big Grab" since it could transfer enormous amounts of shareholder wealth to top managers.<sup>1</sup> At the time the 2014 Equity Plan was proposed, the potential value of the 16.6% dilution from all Coca-Cola equity compensation plans was approximately \$24 billion.<sup>2</sup>



**Coca-Cola's equity grants still favor management at the expense of shareholders.**

After the 2014 shareholder vote, it became clear that many, including Warren Buffett, Chairman and CEO of Coca-Cola's largest shareholder, agreed with Wintergreen that the 2014 Equity Plan was flawed, excessive, and called for too much stock issuance. Mr. Buffett also noted that Wintergreen had performed a service by bringing it to the public's attention.<sup>3</sup> As a result, on October 1, 2014, Coca-Cola announced it would implement guidelines to reduce the potential dilution caused by the 2014 Equity Plan.<sup>4</sup>

This year, Coca-Cola's proxy shows improved disclosure about pay, and it has halted the massive potential dilution – what Wintergreen calls the Big Grab. But we believe Coca-Cola's equity grants – and the criteria used to award them – still favor management at the expense of shareholders.

### Board of Directors

On July 23, 2014 Wintergreen called for new directors to provide fresh thinking and lead a turnaround at Coca-Cola.

We were pleased that on February 19, 2015, the company announced it would add two new directors and that two long-serving members would retire from the board. It is a step in the right direction; however, we believe the current board remains entrenched.

### A Bargain Buyout?

On June 17, 2014 Wintergreen warned of a potential Heinz-style bargain buyout of Coca-Cola based on news reports that 3G Capital and Berkshire Hathaway might be considering a large deal.

Although pundits initially dismissed the idea of a Coca-Cola buyout, a report on October 29, 2014 by analysts at Nomura Securities said a deal is possible and would offer opportunities to increase Coca-Cola's operating income by over \$11 billion per year.<sup>5</sup>

Coca-Cola Chairman and CEO Muhtar Kent might have the possibility of a buyout in mind, telling the Wall Street Journal, "If we don't do what we need to do quickly, effective, execute 100 percent, then somebody else will come and do it for us."<sup>6</sup>

Other consumer-goods companies such as Heinz and Kraft are taking dramatic steps to reduce costs and improve margins and profitability. Why isn't Coca-Cola doing the same? Coca-Cola expects \$3.6 billion in annual savings by 2019<sup>7</sup>, a target Wintergreen views as far too low given Coca-Cola's \$17 billion in annual SG&A expenses.<sup>8</sup> And in a twist straight out of its tired old playbook, Coca-Cola plans to spend the savings on more marketing.<sup>9</sup> To us, that's no savings at all.

### Management Accountability

Wintergreen has also looked closely at the performance of investments made by Coca-Cola under the leadership of Chairman and CEO Muhtar Kent. In December 2014 Wintergreen released a report that said Coca-Cola's investment in Coca-Cola Enterprises' (CCE) North America bottling assets appeared to be a "massively expensive blunder," but Coca-Cola's lack of disclosure made it difficult to know for sure.<sup>10</sup>

It appears we were right. A short time later, on a December 15, 2014 conference call with investors, Coca-Cola CFO Kathy Waller acknowledged that the company expects to earn essentially zero return on its \$13 billion investment in CCE over the course of approximately a decade, from the 2010 acquisition to 2020.<sup>11</sup>

While we are gratified that Coca-Cola confirmed our analysis, it appears to us that neither Muhtar Kent nor anyone else in top management at Coca-Cola has been held accountable for this investment.

### Corporate Revitalization

Last year, Wintergreen called for a sweeping restructuring to improve shareholder value at Coca-Cola, noting that the company's profit margins were well below those of other global consumer packaged goods businesses and its announced cost-cutting plan was well short of what could be done.<sup>12</sup>

Although Coca-Cola now recognizes it needs to restructure, a turnaround remains far away. Announcing Coca-Cola's 2014 year-end earnings, Muhtar Kent said 2015 will be "a transition year" – a term used nine times in the company's 2015 proxy – and per-share earnings growth would be in the mid-single digits.<sup>13</sup>



**Shareholders  
deserve better.  
We believe  
Coca-Cola's cost-  
cutting targets  
are far too low.**

Coca-Cola's problems appear to Wintergreen to be a direct result of the failings of Muhtar Kent and his management team. While he has been CEO, Muhtar Kent has overseen the following:

- The seemingly failed acquisition of CCE North America for \$13 billion.
- The acquisition of expensive minority interests in Monster Beverage and Keurig Green Mountain for several billion dollars.
- A failure to foresee the significant changes in consumer tastes that are upending the beverage business.
- The saddling of Coca-Cola's balance sheet with over \$30 billion of additional debt in an attempt to rekindle growth.<sup>14</sup>

We believe there would be no need for a "transition year" if Muhtar Kent had not made so many costly mistakes over the past eight years. Shareholders deserve better, and the Coca-Cola board must pursue a more ambitious restructuring plan. The transformative strategies implemented at Heinz and newly underway at Kraft should be driving the Coca-Cola board to action.

## Assessing Coca-Cola's 2015 Proxy Statement

Coca-Cola's 2015 Proxy Statement contains better disclosure than a year ago regarding the value of equity incentive compensation and required performance hurdles for management. Importantly, it shows Coca-Cola did not issue secret bonus shares – the much-criticized stock awards granted without criteria.<sup>15</sup>

While that is good news for shareholders, the proxy statement shows Coca-Cola is falling short in other important areas. We believe the company's 2015 proxy statement:

- Contains a misleading characterization of CEO Muhtar Kent's pay (page 3)
- Shows missed performance targets that were apparently overlooked when awarding pay for top managers (page 51)
- Lowers performance hurdles for management in 2015 versus 2014 (page 52)
- Understates the dilutive effect of Coke's equity compensation awards (pages 10 and 46)
- Raises questions about the directors' ability to be forceful advocates for all shareholders



**Muhtar Kent said  
2015 will be a  
"transition year"**

Coca-Cola failed to meet two out of three of their annual performance targets, and met only the very bottom end of the third -

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### COCA-COLA EXECUTIVES MOSTLY MISSED THEIR TARGETS

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2014 Performance Factor	2014 Target	2014 Actual
EPS Growth	7-9%	<b>5.5%</b>
Operating Income Growth	6-8%	<b>6.0%</b>
Case Volume Growth	3-4%	<b>1.5%</b>

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Source: Coca-Cola Company 2015 proxy statement, page 51

Yet Coca-Cola's board has seemingly failed to hold Chairman and CEO Muhtar Kent accountable for this. Coca-Cola's proxy statement says Muhtar Kent "respectfully declined" his annual incentive award, suggesting he took a meaningful pay cut.<sup>16</sup> In fact, the board increased his stock and option awards, making his total pay about even with 2014.<sup>17</sup>

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### MUHTAR KENT'S ILLUSORY PAY CUT

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	2013	2014
Cash salary	\$ 1,600,000	\$ 1,600,000
Stock awards	\$ 6,399,988	\$ 6,489,441
Option awards	\$ 7,113,946	\$ 9,314,144
Non-equity incentives	\$ 2,200,000	\$ -
All other compensation	\$ 861,912	\$ 719,897
Total	\$ 18,175,846	\$ 18,123,482
<b>Reduction (\$)</b>		<b>\$ (52,364)</b>
<b>Reduction (%)</b>		<b>-0.29%</b>

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Source: Coca-Cola Company 2015 proxy statement, page 60

Coca-Cola’s management not only failed to meet its performance targets in 2014, but the 2015 proxy shows the Coca-Cola board has lowered the 2015 performance bar<sup>18</sup> for the coming year, making it easier for management to earn their annual bonuses.

### 2015 vs 2014 PERFORMANCE TARGETS<sup>19</sup>

	2014	2015	CHANGE
Profit Growth	6-8%	4-5%	▼ 36%
Case Volume Growth	3-4%	2-3%	▼ 29%
Revenue Growth	—	3-4%	—

Source: Coca-Cola Company 2015 proxy statement, page 52, and 2014 proxy statement, page 54

What’s more, the calculation of one important metric – unit case volume growth – seemingly includes sales by the Monster Beverage joint venture, which appears to us to be a low-margin distribution agreement that, in our view, will likely add little to shareholder value but will help Coca-Cola executives meet the volume growth target and earn their annual bonuses.<sup>20</sup>

The Coca-Cola 2015 proxy also understates, in our view, the effect of excessive equity pay by the company.

Coca-Cola touts a figure of “\$4.2 billion in gross share repurchases” on two different locations in their 2015 proxy statement.<sup>21</sup> In our view, this overlooks the fact that, net of dilution from equity compensation, buybacks were only \$2.6 billion in 2014.<sup>22</sup>

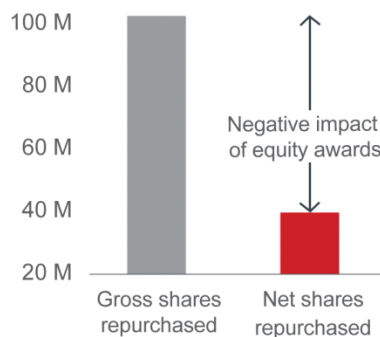
Similarly, the company says it repurchased 98 million shares in 2014, but its shares outstanding only declined by 36 million because of the dilutive effects of equity compensation.<sup>23</sup>



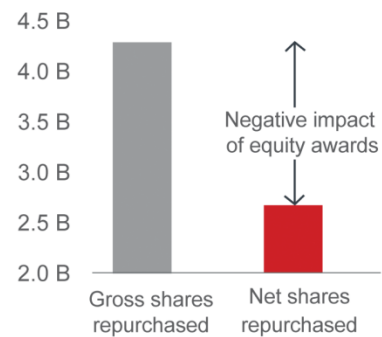
**Many board members have overlapping business interests.**

### UNDERSTATING THE EFFECT OF EQUITY AWARDS

# of shares repurchased



\$ of shares repurchased



A close review of the 2015 Coca-Cola proxy statement also raises questions in our mind about whether the Coca-Cola directors can be effective guardians of the interests of all Coca-Cola shareholders.

Many board members have overlapping business interests, and several have business ties with investment bank Allen & Co. - whose CEO is Coca-Cola director Herbert Allen. Wintergreen believes these business ties can make the board an insular club rather than a vigilant protector of shareholders' interests.

## Conclusion

While Coca-Cola has begun to make progress on the issues identified by Wintergreen beginning a year ago, much more needs to be done, and urgently. If Coca-Cola were a well-run company, we believe the shares could be worth much more. The company's problems are fixable. We believe fixing Coca-Cola requires:

- Improved management, likely from outside the Coca-Cola system
- An aggressive, comprehensive turnaround plan
- A sense of urgency on the part of management and the Board of Directors
- A Board of Directors that will challenge management and hold them accountable
- Improved corporate governance and disclosure practices

Wintergreen believes significant change is needed at Coca-Cola, led by either its current management and board of directors or others. Coca-Cola's day of reckoning is approaching.

Wintergreen plans to vote against Coca-Cola's directors. In our view, they have not exhibited the leadership and independence needed to restore shareholder confidence and return the company to profitable growth. We urge shareholders to carefully review the directors' actions with regard to awarding executive compensation, setting business performance targets and making forthright disclosures to shareholders.



## About Wintergreen Advisers

Established in 2005, Wintergreen is an independent global money manager that employs a research-driven value style in managing global securities. As of March 31, 2015, Wintergreen Advisers had approximately \$1.5 billion under management on behalf of individuals and institutions through its mutual fund and other clients, and is based in Mountain Lakes, New Jersey. As of December 31, 2014, Wintergreen's clients owned over 2.5 million shares of The Coca-Cola Company, and have owned Coca-Cola shares for over five years. For further information on Wintergreen Advisers, please call 973-263-4500 or visit [www.wintergreenadvisers.com](http://www.wintergreenadvisers.com).

Additional information regarding what we view as the issues at The Coca-Cola Company may be found at [www.FixBigSoda.com](http://www.FixBigSoda.com). For information, forms and documents regarding our U.S. mutual fund, please visit [www.wintergreenfund.com](http://www.wintergreenfund.com).

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- 1 "Coca-Cola's Big Grab: Enriching Management, Shortchanging Shareholders," Wintergreen Advisers presentation and webcast, April 2, 2014.
  - 2 See page 86 of Coca-Cola's 2014 proxy statement. Based on total shares outstanding as of 2/24/14.
  - 3 Warren Buffett interviews on CNBC with Becky Quick, April 23, 2014 and March 2, 2015.
  - 4 The Coca-Cola Company 2014 Equity Plan Equity Stewardship Guidelines, October 1, 2014.
  - 5 "The Coca-Cola Company: Reassessing the Self-Help Story," Nomura Securities, Global Equity Research, October 29, 2014.
  - 6 "What is Coke CEO's Solution for Lost Fizz? More Soda," The Wall Street Journal, March 18, 2015.
  - 7 Coca-Cola 2014 10-K report, page 53.
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  - 10 Coca-Cola's Fizzy Math: How Bad Performance, Excessive Pay and Weak Governance are Harming Shareholders," Wintergreen Advisers, December 2014.
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  - 13 Coca-Cola earnings release and investor conference call, February 10, 2015.
  - 14 Bloomberg. Change in Coca-Cola's debt from year-end 2008 to year-end 2014.
  - 15 Wintergreen Asks Coca-Cola to Retract Management Share Awards,' The Wall Street Journal, February 3, 2015.
  - 16 Coca-Cola 2015 proxy statement, page 3.
  - 17 Coca-Cola 2015 proxy statement, page 60.
  - 18 Coca-Cola Company 2015 proxy statement, page 52; 2014 proxy statement, page 54.
  - 19 Change from prior years is calculated at the mid-point average. See the Coca-Cola 2015 proxy statement, page 52, and the Coca-Cola 2014 proxy statement for profit and volume growth targets. Earnings per share growth was used in 2014, but replaced with revenue growth for 2015.
  - 20 The Coca-Cola Company and Monster Beverage Corporation Enter into Long-Term Strategic Partnership," Coca-Cola Company press release, August 14, 2014.
  - 21 Coca-Cola 2015 proxy statement, pages 10 and 46.
  - 22 Coca-Cola Company February 10, 2015 press release, page 3.
  - 23 Coca-Cola Company 10k statement, page 77.