

## ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

### Overview

The following Management's Discussion and Analysis of Financial Condition and Results of Operations ("MD&A") is intended to help the reader understand The Coca-Cola Company, our operations and our present business environment. MD&A is provided as a supplement to—and should be read in conjunction with—our consolidated financial statements and the accompanying notes thereto contained in "Item 8. Financial Statements and Supplementary Data" of this report. This overview summarizes the MD&A, which includes the following sections:

- *Our Business* — a general description of our business and the nonalcoholic beverages segment of the commercial beverages industry; our objective; our areas of focus; and challenges and risks of our business.
- *Critical Accounting Policies and Estimates* — a discussion of accounting policies that require critical judgments and estimates.
- *Operations Review* — an analysis of our Company's consolidated results of operations for the three years presented in our consolidated financial statements. Except to the extent that differences among our operating segments are material to an understanding of our business as a whole, we present the discussion in the MD&A on a consolidated basis.
- *Liquidity, Capital Resources and Financial Position* — an analysis of cash flows; off-balance sheet arrangements and aggregate contractual obligations; foreign exchange; an overview of financial position; and the impact of inflation and changing prices.

### Our Business

#### *General*

We are the largest manufacturer, distributor and marketer of nonalcoholic beverage concentrates and syrups in the world. Along with Coca-Cola, which is recognized as the world's most valuable brand, we market four of the world's top five nonalcoholic sparkling brands, including Diet Coke, Fanta and Sprite. Our Company owns or licenses more than 400 brands, including diet and light beverages, waters, juice and juice drinks, teas, coffees, and energy and sports drinks. Through the world's largest beverage distribution system, consumers in more than 200 countries enjoy the Company's beverages at a rate exceeding 1.4 billion servings each day. Our Company generates revenues, income and cash flows by selling beverage concentrates and syrups as well as some finished beverages. We generally sell these products to bottling and canning operations, fountain wholesalers and some fountain retailers and, in the case of finished products, to distributors. Our bottlers sell our branded products to businesses and institutions including retail chains, supermarkets, restaurants, small neighborhood grocers, sports and entertainment venues, and schools and colleges. We continue to expand our marketing presence and increase our unit case volume in most developing and emerging markets. Our strong and stable system helps us to capture growth by manufacturing, distributing and marketing existing, enhanced and new innovative products to our consumers throughout the world.

We have three types of bottling relationships: bottlers in which our Company has no ownership interest, bottlers in which our Company has a noncontrolling ownership interest and bottlers in which our Company has a controlling ownership interest. We authorize our bottling partners to manufacture and package products made from our concentrates and syrups into branded finished products that they then distribute and sell. In 2006, bottling partners in which our Company has no ownership interest or a noncontrolling ownership interest produced and distributed approximately 83 percent of our worldwide unit case volume.

We make significant marketing expenditures in support of our brands, including expenditures for advertising, sponsorship fees and special promotional events. As part of our marketing activities, we, at our discretion, provide retailers and distributors with promotions and point-of-sale displays; our bottling partners with advertising support and funds designated for the purchase of cold-drink equipment; and our consumers with coupons, discounts and promotional incentives. These marketing expenditures help to enhance awareness of and increase consumer preference for our brands. We believe that greater awareness and preference promotes long-term growth in unit case volume, per capita consumption and our share of worldwide nonalcoholic beverage sales.

### *The Nonalcoholic Beverages Segment of the Commercial Beverages Industry*

We operate in the highly competitive nonalcoholic beverages segment of the commercial beverages industry. We face strong competition from numerous other general and specialty beverage companies. We, along with other beverage companies, are affected by a number of factors, including, but not limited to, cost to manufacture and distribute products, consumer spending, economic conditions, availability and quality of water, consumer preferences, inflation, political climate, local and national laws and regulations, foreign currency exchange fluctuations, fuel prices and weather patterns.

### *Our Objective*

Our objective is to use our formidable assets—brands, financial strength, unrivaled distribution system, global reach, and a strong commitment by our management and employees worldwide—to achieve long-term sustainable growth. Our vision for sustainable growth includes the following:

- People: Being a great place to work where people are inspired to be the best they can be.
- Portfolio: Bringing to the world a portfolio of beverage brands that anticipates and satisfies people's desires and needs.
- Partners: Nurturing a winning network of partners and building mutual loyalty.
- Planet: Being a responsible global citizen that makes a difference.
- Profit: Maximizing return to shareowners while being mindful of our overall responsibilities.

### *Areas of Focus*

We intend to continue to strengthen our capabilities in consumer marketing, customer and commercial leadership, and franchise leadership to create long-term sustainable growth for our Company and the Coca-Cola system and value for our shareowners.

### *Consumer Marketing*

Marketing investments are designed to enhance consumer awareness and increase consumer preference for our brands. This produces long-term growth in unit case volume, per capita consumption and our share of worldwide nonalcoholic beverage sales. We heighten consumer awareness of and product appeal for our brands using integrated marketing programs. Through our relationships with our bottling partners and those who sell our products in the marketplace, we create and implement marketing programs both globally and locally. In developing a strategy for a Company brand, we conduct product and packaging research, establish brand positioning, develop precise consumer communications and solicit consumer feedback. Our integrated global and local marketing programs include activities such as advertising, point-of-sale merchandising and sales promotions.

### *Customer and Commercial Leadership*

The Coca-Cola system has millions of customers around the world who sell or serve our products directly to consumers. We focus on enhancing value for our customers and providing solutions to grow their beverage businesses. Our approach includes understanding each customer's business and needs, whether that customer is a sophisticated retailer in a developed market or a kiosk owner in an emerging market. We focus on ensuring that our customers have the right product and package offerings and the right promotional tools to deliver enhanced value to themselves and the Company. We are constantly looking to build new beverage consumption occasions in our customers' outlets through unique and innovative consumer experiences, product availability and delivery systems, and beverage merchandising and displays.

### *Franchise Leadership*

We are renewing our franchise leadership to give our Company and our bottling partners the ability to grow together through shared values, aligned incentives and a sense of urgency and flexibility that supports consumers' always changing needs and tastes. The financial health and success of our bottling partners are critical components of the Company's success. We work with our bottling partners to continuously look for ways to improve system economics, and we share best practices throughout the bottling system. We also design business models for still beverages in specific markets to ensure that we appropriately share the value created by these beverages with our bottling partners. We will continue to build a supply chain network that leverages the size and scale of the Coca-Cola system to gain a competitive advantage.

### *Challenges and Risks*

Being a global company provides unique opportunities for our Company. Challenges and risks accompany those opportunities.

Our management has identified certain challenges and risks that demand the attention of the nonalcoholic beverages segment of the commercial beverages industry and our Company. Of these, four key challenges and risks are discussed below.

*Obesity and Inactive Lifestyles.* Increasing awareness among consumers, public health professionals and government agencies of the potential health problems associated with obesity and inactive lifestyles represents a significant challenge to our industry. We recognize that obesity is a complex public health problem. Our commitment to consumers begins with our broad product line, which includes a wide selection of diet and light beverages, juice and juice drinks, sports drinks and water products. Our commitment also includes adhering to responsible policies in schools and in the marketplace; supporting programs to encourage physical activity and promote nutrition education; and continuously meeting changing consumer needs through beverage innovation, choice and variety. We are committed to playing an appropriate role in helping address this issue in cooperation with governments, educators and consumers through science-based solutions and programs.

*Water Quality and Quantity.* Water quality and quantity is an issue that increasingly requires our Company's attention and collaboration with the nonalcoholic beverages segment of the commercial beverages industry, governments, nongovernmental organizations and communities where we operate. Water is the main ingredient in substantially all of our products. It is also a limited natural resource facing unprecedented challenges from overexploitation, increasing pollution and poor management. Our Company is in an excellent position to share the water-related knowledge we have developed in the communities we serve—water-resource management, water treatment, wastewater treatment systems, and models for working with communities and partners in addressing water and sanitation needs. We are actively engaged in assessing the specific water-related risks that we and many of our bottling partners face and have implemented a formal water risk management program. We are working with our global partners to develop water sustainability projects. We are actively encouraging improved water efficiency and conservation efforts throughout our system. As demand for water

continues to increase around the world, we expect commitment and continued action on our part will be crucial in the successful long-term stewardship of this critical natural resource.

*Evolving Consumer Preferences.* Consumers want more choices. We are impacted by shifting consumer demographics and needs, on-the-go lifestyles, aging populations in developed markets and consumers who are empowered with more information than ever. We are committed to generating new avenues for growth through our core brands with a focus on diet and light products. We are also committed to continuing to expand the variety of choices we provide to consumers to meet their needs, desires and lifestyle choices.

*Increased Competition and Capabilities in the Marketplace.* Our Company is facing strong competition from some well-established global companies and many local players. We must continue to selectively expand into other profitable segments of the nonalcoholic beverages segment of the commercial beverages industry and strengthen our capabilities in marketing and innovation in order to maintain our brand loyalty and market share.

All four of these challenges and risks—obesity and inactive lifestyles, water quality and quantity, evolving consumer preferences and increased competition and capabilities in the marketplace—have the potential to have a material adverse effect on the nonalcoholic beverages segment of the commercial beverages industry and on our Company; however, we believe our Company is well positioned to appropriately address these challenges and risks.

See also “Item 1A. Risk Factors” in Part I of this report for additional information about risks and uncertainties facing our Company.

### **Critical Accounting Policies and Estimates**

Our consolidated financial statements are prepared in accordance with generally accepted accounting principles in the United States, which require management to make estimates, judgments and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. We believe that our most critical accounting policies and estimates relate to the following:

- Basis of Presentation and Consolidation
- Recoverability of Noncurrent Assets
- Revenue Recognition
- Income Taxes
- Contingencies

Management has discussed the development, selection and disclosure of critical accounting policies and estimates with the Audit Committee of the Company’s Board of Directors. While our estimates and assumptions are based on our knowledge of current events and actions we may undertake in the future, actual results may ultimately differ from these estimates and assumptions. For a discussion of the Company’s significant accounting policies, refer to Note 1 of Notes to Consolidated Financial Statements.

#### ***Basis of Presentation and Consolidation***

In December 2003, the Financial Accounting Standards Board (“FASB”) issued Interpretation No. 46(R). We adopted Interpretation No. 46(R) effective April 2, 2004. Refer to Note 1 of Notes to Consolidated Financial Statements.

Our Company consolidates all entities that we control by ownership of a majority voting interest as well as variable interest entities for which our Company is the primary beneficiary. Our judgment in determining if we are the primary beneficiary of the variable interest entities includes assessing our Company’s level of involvement in setting up the entity, determining if the activities of the entity are substantially conducted on

behalf of our Company, determining whether the Company provides more than half of the subordinated financial support to the entity, and determining if we absorb the majority of the entity's expected losses or returns.

We use the equity method to account for investments for which we have the ability to exercise significant influence over operating and financial policies. Our consolidated net income includes our Company's share of the net earnings of these companies. Our judgment regarding the level of influence over each equity method investment includes considering key factors such as our ownership interest, representation on the board of directors, participation in policy-making decisions and material intercompany transactions.

We use the cost method to account for investments in companies that we do not control and for which we do not have the ability to exercise significant influence over operating and financial policies. In accordance with the cost method, these investments are recorded at cost or fair value, as appropriate. We record dividend income when applicable dividends are declared.

Our Company eliminates from financial results all significant intercompany transactions, including the intercompany portion of transactions with equity method investees.

#### ***Recoverability of Noncurrent Assets***

Management's assessments of the recoverability of noncurrent assets involve critical accounting estimates. These assessments reflect management's best assumptions, which, when appropriate, are consistent with the assumptions that we believe hypothetical marketplace participants would use. Factors that management must estimate when performing recoverability and impairment tests include, among others, sales volume, prices, inflation, cost of capital, marketing spending, foreign currency exchange rates, tax rates and capital spending. These factors are often interdependent and therefore do not change in isolation. These factors include inherent uncertainties, and significant management judgment is involved in estimating their impact. However, when appropriate, the assumptions we use for financial reporting purposes are consistent with those we use in our internal planning and we believe are consistent with those that a hypothetical marketplace participant would use. Management periodically evaluates and updates the estimates based on the conditions that influence these factors. The variability of these factors depends on a number of conditions, including uncertainty about future events, and thus our accounting estimates may change from period to period. If other assumptions and estimates had been used in the current period, the balances for noncurrent assets could have been materially impacted. Furthermore, if management uses different assumptions or if different conditions occur in future periods, future operating results could be materially impacted.

Our Company faces many uncertainties and risks related to various economic, political and regulatory environments in the countries in which we operate. Refer to the heading "Our Business—Challenges and Risks," above, and "Item 1A. Risk Factors" in Part I of this report. As a result, management must make numerous assumptions which involve a significant amount of judgment when determining the recoverability of noncurrent assets in various regions around the world.

For the noncurrent assets listed in the table below, we perform tests of impairment as appropriate. For applicable assets, we perform these tests when certain conditions exist that indicate the carrying value may not

be recoverable. For other applicable assets, we perform these tests at least annually or more frequently if events or circumstances indicate that an asset may be impaired:

December 31, 2006	Carrying Value	Percentage of Total Assets
(In millions except percentages)		
Tested for impairment when conditions exist that indicate carrying value may be impaired:		
Equity method investments	\$ 6,310	21%
Cost method investments, principally bottling companies	473	2
Other assets	2,701	9
Property, plant and equipment, net	6,903	23
Amortized intangible assets, net (various, principally trademarks)	198	0
Total	<u>\$ 16,585</u>	<u>55%</u>
Tested for impairment at least annually or when events indicate that an asset may be impaired:		
Trademarks with indefinite lives	\$ 2,045	7%
Goodwill	1,403	5
Bottlers' franchise rights	1,359	5
Other intangible assets not subject to amortization	130	0
Total	<u>\$ 4,937</u>	<u>17%</u>

Many of the noncurrent assets listed above are located in markets that we consider to be developing or to have changing political environments. These markets include, but are not limited to, the Middle East and Egypt, where political and civil unrest continues; the Philippines, where affordability and availability of beverages in the marketplace continue to impact operating results; India, where affordability issues remain; and certain markets in Latin America, Asia and Africa, where local economic and political conditions are unstable. We have bottling assets and investments in many of these markets. The table below reflects the Company's carrying value of noncurrent assets in these markets.

December 31, 2006	Carrying Value	Percentage of Applicable Line Item Above
(In millions except percentages)		
Tested for impairment when conditions exist that indicate carrying value may be impaired:		
Equity method investments	\$ 533	8%
Cost method investments, principally bottling companies	123	26
Other assets	83	3
Property, plant and equipment, net	2,150	31
Amortized intangible assets, net (various, principally trademarks)	11	6
Total	<u>\$ 2,900</u>	<u>17</u>
Tested for impairment at least annually or when events indicate that an asset may be impaired:		
Trademarks with indefinite lives	\$ 394	19%
Goodwill	—	0
Bottlers' franchise rights	52	4
Other intangible assets not subject to amortization	23	18
Total	<u>\$ 469</u>	<u>9</u>

### *Equity Method and Cost Method Investments*

We review our equity and cost method investments in every reporting period to determine whether a significant event or change in circumstances has occurred that may have an adverse effect on the fair value of each investment. When such events or changes occur, we evaluate the fair value compared to the carrying value of the related investment. We also perform this evaluation every reporting period for each investment for which the carrying value has exceeded the fair value in the prior period. The fair values of most of our Company's investments in publicly traded companies are often readily available based on quoted market prices. For investments in nonpublicly traded companies, management's assessment of fair value is based on valuation methodologies including discounted cash flows, estimates of sales proceeds and external appraisals, as appropriate. We consider the assumptions that we believe hypothetical marketplace participants would use in evaluating estimated future cash flows when employing the discounted cash flow or estimate of sales proceeds valuation methodologies. The ability to accurately predict future cash flows, especially in developing and unstable markets, may impact the determination of fair value.

In the event a decline in fair value of an investment occurs, management may be required to determine if the decline in fair value is other than temporary. Management's assessment as to the nature of a decline in fair value is based on the valuation methodologies discussed above, our ability and intent to hold the investment, and whether evidence indicating the cost of the investment is recoverable within a reasonable period of time outweighs evidence to the contrary. We consider most of our equity method investees to be strategic long-term investments. If the fair value of an investment is less than its carrying value and the decline in value is considered to be other than temporary, a write-down is recorded. Management's assessments of fair value represent our best estimates as of the time of the impairment review and are consistent with the assumptions that we believe hypothetical marketplace participants would use. If different assessments were made, this could have a material impact on our consolidated financial statements.

The following table presents the difference between calculated fair values, based on quoted closing prices of publicly traded shares, and our Company's carrying values for significant investments in publicly traded bottlers accounted for as equity method investees (in millions):

December 31, 2006	Fair Value	Carrying Value	Difference
Coca-Cola Enterprises Inc.	\$ 3,450	\$ 1,312 <sup>1</sup>	\$ 2,138
Coca-Cola Hellenic Bottling Company S.A.	2,247	1,251	996
Coca-Cola FEMSA, S.A.B. de C.V.	2,172	835	1,337
Coca-Cola Amatil Limited	1,456	817	639
Coca-Cola Icecek A.S.	372	110	262
Grupo Continental, S.A.	327	165	162
Coca-Cola Embonor S.A.	228	189	39
Coca-Cola Bottling Company Consolidated	170	68	102
Embotelladoras Polar S.A.	93	59	34
	\$ 10,515	\$ 4,806	\$ 5,709

<sup>1</sup> In 2006, our carrying value of CCE was reduced by our proportionate share of an impairment charge recorded by CCE. Refer to Note 3 of Notes to Consolidated Financial Statements.

### *Other Assets*

Our Company invests in infrastructure programs with our bottlers that are directed at strengthening our bottling system and increasing unit case volume. Additionally, our Company advances payments to certain customers to fund future marketing activities intended to generate profitable volume and expenses such payments over the periods benefited. Advance payments are also made to certain customers for distribution rights. Payments under these programs are generally capitalized and reported as other assets in our consolidated

balance sheets. Management evaluates the recoverability of the carrying value of these assets when facts and circumstances indicate that the carrying value of these assets may not be recoverable by preparing estimates of sales volume and the resulting gross profit and cash flows. If the carrying value of these assets is assessed to be recoverable, it is amortized over the periods benefited. If the carrying value of these assets is considered to be not recoverable, an impairment is recognized, resulting in a write-down of assets.

#### *Property, Plant and Equipment*

Certain events or changes in circumstances may indicate that the recoverability of the carrying amount of property, plant and equipment should be assessed. Such events or changes may include a significant decrease in market value, a significant change in the business climate in a particular market, or a current-period operating or cash flow loss combined with historical losses or projected future losses. If an event occurs or changes in circumstances are present, we estimate the future cash flows expected to result from the use of the asset and its eventual disposition. If the sum of the expected future cash flows (undiscounted and without interest charges) is less than the carrying amount, we recognize an impairment loss. The impairment loss recognized is the amount by which the carrying amount exceeds the fair value.

#### *Goodwill, Trademarks and Other Intangible Assets*

Statement of Financial Accounting Standards (“SFAS”) No. 142, “Goodwill and Other Intangible Assets,” classifies intangible assets into three categories: (1) intangible assets with definite lives subject to amortization; (2) intangible assets with indefinite lives not subject to amortization; and (3) goodwill. For intangible assets with definite lives, tests for impairment must be performed if conditions exist that indicate the carrying value may not be recoverable. For intangible assets with indefinite lives and goodwill, tests for impairment must be performed at least annually or more frequently if events or circumstances indicate that assets might be impaired. Our equity method investees also perform such tests for impairment for intangible assets and/or goodwill. If an impairment charge was recorded by one of our equity method investees, the Company would record its proportionate share of such charge.

In 2006, our Company recorded a charge of approximately \$602 million in the line item equity income—net resulting from the impact of our proportionate share of an impairment charge recorded by CCE, which impacted Bottling Investments. Refer to the heading “Operations Review—Equity Income—Net” and Note 3 of Notes to Consolidated Financial Statements.

Our trademarks and other intangible assets determined to have definite lives are amortized over their useful lives. In accordance with SFAS No. 142, if conditions exist that indicate the carrying value may not be recoverable, we review such trademarks and other intangible assets with definite lives for impairment to ensure they are appropriately valued. Such conditions may include an economic downturn in a market or a change in the assessment of future operations. Trademarks and other intangible assets determined to have indefinite useful lives are not amortized. We test such trademarks and other intangible assets with indefinite useful lives for impairment annually, or more frequently if events or circumstances indicate that assets might be impaired. Goodwill is not amortized. We also perform tests for impairment of goodwill annually, or more frequently if events or circumstances indicate it might be impaired. All goodwill is assigned to reporting units, which are one level below our operating segments. Goodwill is assigned to the reporting unit that benefits from the synergies arising from each business combination. We perform our impairment tests of goodwill at our reporting unit level. Impairment tests for goodwill include comparing the fair value of the respective reporting unit with its carrying value, including goodwill. We use a variety of methodologies in conducting these impairment assessments, including cash flow analyses that, when appropriate, are consistent with the assumptions we believe hypothetical marketplace participants would use, estimates of sales proceeds and independent appraisals. Where applicable, we use an appropriate discount rate based on the Company’s cost of capital rate or location-specific economic factors.

In 2006, our Company recorded impairment charges of approximately \$41 million primarily related to trademarks for beverages sold in the Philippines and Indonesia. The Philippines and Indonesia are components of East, South Asia and Pacific Rim. The amount of these impairment charges was determined by comparing the fair values of the intangible assets to their respective carrying values. The fair values were determined using discounted cash flow analyses. Because the fair values were less than the carrying values of the assets, we recorded impairment charges to reduce the carrying values of the assets to their respective fair values. These impairment charges were recorded in the line item other operating charges in the consolidated statement of income.

In December 2006, the Company entered into a purchase agreement with San Miguel Corporation and two of its subsidiaries (collectively, “SMC”) to acquire all of the shares of capital stock of Coca-Cola Bottlers Philippines, Inc. (“CCBPI”) held by SMC, representing 65 percent of all the issued and outstanding capital stock of CCBPI. CCBPI is the Company’s authorized bottler in the Philippines. The transaction is subject to certain conditions. Upon the closing of this transaction, the Company will own 100 percent of the issued and outstanding capital stock of CCBPI. Management will continue to monitor the Philippines and conduct impairment reviews as required.

In 2005, our Company recorded impairment charges of approximately \$84 million related to intangible assets. These intangible assets related to trademarks for beverages sold in the Philippines. The carrying value of our trademarks in the Philippines, prior to the recording of the impairment charges in 2005, was approximately \$268 million. The impairments were the result of our revised outlook for the Philippines, which had been unfavorably impacted by declines in volume and income before income taxes resulting from the continued lack of an affordable package offering and the continued limited availability of these trademark beverages in the marketplace. We determined the amounts of the impairment charges by comparing the fair values of the intangible assets to their then carrying values. Fair values were derived using discounted cash flow analyses with a number of scenarios that were weighted based on the probability of different outcomes. Because the fair values were less than the carrying values of the assets, we recorded impairment charges to reduce the carrying values of the assets to fair values. In addition, in 2005, we recorded an impairment charge of approximately \$4 million in the line item equity income—net related to our proportionate share of a write-down of intangible assets recorded by our equity method investee bottler in the Philippines.

In 2004, our Company recorded impairment charges related to intangible assets of approximately \$374 million, primarily related to franchise rights at CCEAG. CCEAG is a component of Bottling Investments. The CCEAG impairment charges were the result of our revised outlook for the German market, which was unfavorably impacted by volume declines resulting from market shifts related to the deposit law on nonrefillable beverage packages and the corresponding lack of availability of our products in the discount retail channel. The deposit law in Germany had led to discount chains creating proprietary nonrefillable packages that could only be returned to their own stores. We determined the amount of the impairment by comparing the fair value of the intangible assets to its then carrying value. Fair values were derived using discounted cash flow analyses with a number of scenarios that were weighted based on the probability of different outcomes. Because the fair value was less than the carrying value of the assets, we recorded an impairment charge to reduce the carrying value of the assets to fair value. These impairment charges were recorded in the line item other operating charges in our consolidated statement of income for 2004. At the end of 2004, the German government passed an amendment to the mandatory deposit legislation that requires retailers, including discount chains, to accept returns of each type of nonrefillable beverage package they sell, regardless of where the beverage package type was purchased. In addition, the mandatory deposit requirement was expanded to other beverage categories.

In August 2006, the Company announced that it had reached an agreement in principle with its independent bottlers in Germany regarding the creation of a single bottler. A non-binding letter of intent was signed containing the financial framework and the key conditions under which CCEAG and the seven independent bottlers will become one bottler. We currently expect that this consolidation will occur in 2007. The Company will be the majority owner of the consolidated bottling operation in Germany. The Company has

considered and will continue to consider the effect of these future structural changes on the recoverability of noncurrent assets and investments in bottling operations in Germany.

### ***Revenue Recognition***

We recognize revenue when persuasive evidence of an arrangement exists, delivery of products has occurred, the sales price is fixed or determinable, and collectibility is reasonably assured. For our Company, this generally means that we recognize revenue when title to our products is transferred to our bottling partners, resellers or other customers. In particular, title usually transfers upon shipment to or receipt at our customers' locations, as determined by the specific sales terms of each transaction.

In addition, our customers can earn certain incentives, which are included in deductions from revenue, a component of net operating revenues in the consolidated statements of income. These incentives include, but are not limited to, cash discounts, funds for promotional and marketing activities, volume-based incentive programs and support for infrastructure programs. Refer to Note 1 of Notes to Consolidated Financial Statements. The aggregate deductions from revenue recorded by the Company in relation to these programs, including amortization expense on infrastructure programs, was approximately \$3.8 billion, \$3.7 billion and \$3.6 billion for the years ended December 31, 2006, 2005 and 2004, respectively.

### ***Income Taxes***

In July 2006, the FASB issued FASB Interpretation No. 48, "Accounting for Uncertainty in Income Taxes" ("Interpretation No. 48"). Interpretation No. 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with FASB Statement No. 109, "Accounting for Income Taxes." Interpretation No. 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. Interpretation No. 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. For our Company, Interpretation No. 48 was effective beginning January 1, 2007, and the cumulative effect adjustment will be recorded in the first quarter of 2007. We believe that the adoption of Interpretation No. 48 will not have a material impact on our consolidated financial statements.

Our annual tax rate is based on our income, statutory tax rates and tax planning opportunities available to us in the various jurisdictions in which we operate. Significant judgment is required in determining our annual tax expense and in evaluating our tax positions. We establish reserves at the time we determine it is probable we will be liable to pay additional taxes related to certain matters. We adjust these reserves, including any impact on the related interest and penalties, in light of changing facts and circumstances, such as the progress of a tax audit.

A number of years may elapse before a particular matter for which we have established a reserve is audited and finally resolved. The number of years with open tax audits varies depending on the tax jurisdiction. While it is often difficult to predict the final outcome or the timing of resolution of any particular tax matter, we record a reserve when we determine the likelihood of loss is probable. Such liabilities are recorded in the line item accrued income taxes in the Company's consolidated balance sheets. Settlement of any particular issue would usually require the use of cash. Favorable resolutions of tax matters for which we have previously established reserves are recognized as a reduction to our income tax expense when the amounts involved become known.

Tax law requires items to be included in the tax return at different times than when these items are reflected in the consolidated financial statements. As a result, the annual tax rate reflected in our consolidated financial statements is different than that reported in our tax return (our cash tax rate). Some of these differences are permanent, such as expenses that are not deductible in our tax return, and some differences reverse over time, such as depreciation expense. These timing differences create deferred tax assets and liabilities. Deferred tax assets and liabilities are determined based on temporary differences between the financial reporting and tax

bases of assets and liabilities. The tax rates used to determine deferred tax assets or liabilities are the enacted tax rates in effect for the year in which the differences are expected to reverse. Based on the evaluation of all available information, the Company recognizes future tax benefits, such as net operating loss carryforwards, to the extent that realizing these benefits is considered more likely than not.

We evaluate our ability to realize the tax benefits associated with deferred tax assets by analyzing our forecasted taxable income using both historical and projected future operating results, the reversal of existing temporary differences, taxable income in prior carryback years (if permitted) and the availability of tax planning strategies. A valuation allowance is required to be established unless management determines that it is more likely than not that the Company will ultimately realize the tax benefit associated with a deferred tax asset.

Additionally, undistributed earnings of a subsidiary are accounted for as a temporary difference, except that deferred tax liabilities are not recorded for undistributed earnings of a foreign subsidiary that are deemed to be indefinitely reinvested in the foreign jurisdiction. The Company has formulated a specific plan for reinvestment of undistributed earnings of its foreign subsidiaries which demonstrates that such earnings will be indefinitely reinvested in the applicable tax jurisdictions. Should we change our plans, we would be required to record a significant amount of deferred tax liabilities.

The American Jobs Creation Act of 2004 (the “Jobs Creation Act”) was enacted in October 2004. Among other things, it provided a one-time benefit related to foreign tax credits generated by equity investments in prior years. In 2004, the Company recorded an income tax benefit of approximately \$50 million as a result of this new law. The Jobs Creation Act also included a temporary incentive for U.S. multinationals to repatriate foreign earnings at an approximate 5.25 percent effective tax rate. During 2005, the Company repatriated approximately \$6.1 billion in previously unremitted foreign earnings, with an associated tax liability of approximately \$315 million. The reinvestment requirements of this repatriation are expected to be fulfilled by 2008 and are not expected to require any material change in the nature, amount or timing of future expenditures from what was otherwise expected. Refer to Note 1 and Note 17 of Notes to Consolidated Financial Statements.

The Company’s effective tax rate is expected to be approximately 23 percent in 2007. This estimated tax rate does not reflect the impact of any unusual or special items that may affect our tax rate in 2007.

### *Contingencies*

Our Company is subject to various claims and contingencies, mostly related to legal proceedings. Due to their nature, such legal proceedings involve inherent uncertainties including, but not limited to, court rulings, negotiations between affected parties and governmental actions. Management assesses the probability of loss for such contingencies and accrues a liability and/or discloses the relevant circumstances, as appropriate. Management believes that any liability to the Company that may arise as a result of currently pending legal proceedings or other contingencies will not have a material adverse effect on the financial condition of the Company taken as a whole. Refer to Note 13 of Notes to Consolidated Financial Statements.

### *Recent Accounting Standards and Pronouncements*

Refer to Note 1 of Notes to Consolidated Financial Statements for a discussion of recent accounting standards and pronouncements.

### **Operations Review**

We manufacture, distribute and market nonalcoholic beverage concentrates and syrups. We also manufacture, distribute and market some finished beverages. Our organizational structure as of December 31, 2006 consisted of the following operating segments, the first seven of which are sometimes referred to as “operating groups” or “groups”: Africa; East, South Asia and Pacific Rim; European Union; Latin America; North America; North Asia, Eurasia and Middle East; Bottling Investments; and Corporate. For further information regarding our operating segments, including a discussion of changes made to our operating segments during 2006, refer to Note 20 of Notes to Consolidated Financial Statements.

## Volume

We measure our sales volume in two ways: (1) unit cases of finished products and (2) gallons. A “unit case” is a unit of measurement equal to 192 U.S. fluid ounces of finished beverage (24 eight-ounce servings). Unit case volume represents the number of unit cases of Company beverage products directly or indirectly sold by the Company and its bottling partners (“Coca-Cola system”) to consumers. Unit case volume primarily consists of beverage products bearing Company trademarks. Also included in unit case volume are certain products licensed to, or distributed by, our Company, and brands owned by Coca-Cola system bottlers for which our Company provides marketing support and from the sale of which it derives income. Such products licensed to, or distributed by, our Company or owned by Coca-Cola system bottlers account for a minimal portion of total unit case volume. In addition, unit case volume includes sales by joint ventures in which the Company is a partner. Unit case volume is derived based on estimates supplied by our bottling partners and distributors. A “gallon” is a unit of measurement for concentrates, syrups, beverage bases, finished beverages and powders (in all cases expressed in equivalent gallons of syrup) sold by the Company to its bottling partners or other customers. Most of our revenues are based on gallon sales, a primarily wholesale activity, as discussed under “Item 1. Business” in Part I of this report and the heading “Net Operating Revenues,” below. Unit case volume and gallon sales growth rates are not necessarily equal during any given period. Items such as seasonality, bottlers’ inventory practices, supply point changes, timing of price increases and new product introductions and changes in product mix can impact unit case volume and gallon sales and can create differences between unit case volume and gallon sales growth rates.

Information about our volume growth by operating segment is as follows:

Year Ended December 31,	Percentage Change			
	2006 vs. 2005		2005 vs. 2004	
	Unit Cases <sup>1,2</sup>	Gallons	Unit Cases <sup>1,2</sup>	Gallons
Worldwide	4%	4%	4%	3%
International	6	5	5	4
Africa	4	3	6	7
East, South Asia and Pacific Rim	(5)	(4)	(4)	(6)
European Union	6	4	—	—
Latin America	7	7	6	6
North America	—	—	2	1
North Asia, Eurasia and Middle East	11	7	15	10
Bottling Investments	16	N/A	6	N/A

<sup>1</sup> Bottling Investments segment data reflects unit case volume growth for consolidated bottlers only.

<sup>2</sup> Geographic segment data reflects unit case volume growth for all bottlers in the applicable geographic areas, both consolidated and unconsolidated.

## Unit Case Volume

Although most of our Company’s revenues are not based directly on unit case volume, we believe unit case volume is one of the measures of the underlying strength of the Coca-Cola system because it measures our product trends at the consumer level. The Coca-Cola system sold approximately 21.4 billion unit cases of our products in 2006, approximately 20.6 billion unit cases in 2005, and approximately 19.8 billion unit cases in 2004.

In Africa, unit case volume increased 4 percent in 2006 compared to 2005, reflecting growth across the majority of divisions, which was partially offset by a slight decline in Nigeria primarily related to affordability issues and competitive and economic pressure. The unit case volume increase in Africa was also partially offset

by an industrywide temporary shortage in the supply of carbon dioxide in South Africa in the fourth quarter of 2006.

Unit case volume in East, South Asia and Pacific Rim decreased 5 percent in 2006 versus 2005, primarily due to a double-digit decline in the Philippines, which was mainly driven by the continued impact of affordability and availability issues. In December 2006, the Company and SMC entered into an agreement for the Company to acquire, subject to the fulfillment of certain conditions, the 65 percent ownership interest in CCBPI held by SMC. Upon the closing of the acquisition, the Company will own 100 percent of the issued and outstanding capital stock of CCBPI. The transaction is expected to close during the first quarter of 2007. The Company expects performance in the Philippines to remain weak during 2007. Performance in this operating segment was also impacted by a 5 percent decline in India primarily due to price increases in the second half of 2005 and steps taken to drive revenue growth and improve operating and working capital efficiency. The results in India reflected high single-digit declines in sparkling beverages which was partially offset by growth in still beverages. Continued investment in marketing initiatives around the quality and safety of our products and focus on execution in the consolidated bottling operations delivered positive results during the second half of 2006, despite the renewed unfounded allegations of unsafe pesticide levels in the Company's products.

Unit case volume in the European Union increased 6 percent in 2006 compared to 2005, primarily due to solid growth across all divisions driven by successful marketing campaigns, launches of Coca-Cola Zero in nine countries and favorable weather in the second half of 2006. In addition, the acquisition of Apollinaris GmbH, a German premium source water brand ("Apollinaris"), and the joint acquisition of Fonti del Vulture S.r.l., also known as Traficante, an Italian mineral water company, with Coca-Cola HBC during 2006 contributed approximately 2 percentage points of unit case volume growth in 2006. Unit case volume in Germany increased 5 percent in 2006 versus 2005, and reflected strong growth of Trademark Coca-Cola in 2006 compared to 2005. The results were driven by improved marketplace execution capabilities, the launch of Coca-Cola Zero in July 2006, increased availability in the discounter channel and generally favorable weather. As mentioned above, the acquisition of Apollinaris also contributed to unit case volume growth in Germany. The Company expects stabilizing trends in Germany to continue during 2007. Unit case volume in Northwest Europe increased 3 percent in 2006 versus 2005 as performance stabilized. The results reflected 3 percent unit case volume growth in sparkling beverages, led by growth of Trademark Coca-Cola, and solid growth in still beverages. In addition, the successful launch of Coca-Cola Zero in Great Britain at the end of June 2006 and generally favorable weather during the second half of the year contributed to the performance. Unit case volume in Iberia increased 6 percent in 2006 versus 2005, led by strong growth in Spain.

In Latin America, unit case volume increased 7 percent in 2006 versus 2005, primarily due to growth in sparkling beverages led by growth of Trademark Coca-Cola. This performance was seen in all key markets, especially Brazil, Mexico and Argentina. In Mexico, the increase in unit case volume was driven by strong growth in Trademark Coca-Cola. In Brazil, strong marketing and bottler execution led to unit case volume growth in sparkling beverages. In Argentina, consumer marketing activities and bottler execution drove unit case volume growth. Additionally, in December 2006, the Company and Coca-Cola FEMSA entered into an agreement to jointly acquire Jugos del Valle, S.A.B. de C.V., the second largest producer of packaged juices, nectars and fruit-flavored beverages in Mexico and the largest producer of such products in Brazil.

Unit case volume in North America was even in 2006 versus 2005. Foodservice and Hospitality unit case volume increased 1 percent in 2006, reflecting growth in all key beverage categories. Unit case volume in Retail decreased 1 percent primarily driven by weak sparkling beverage trends in the second half of 2006, declines in the warehouse-delivered water business resulting from the strategic decision to refocus resources behind the more profitable Dasani business and declines in the warehouse-delivered juice business as a result of price increases to cover higher ingredient costs. These declines in Retail were partially offset by the continued success of Dasani, Coca-Cola Zero and Powerade, as well as the introduction of Black Cherry Vanilla Coca-Cola and the national rollout of Vault. In February 2007, our Company entered into an agreement to purchase Fuze

Beverage, LLC, maker of Fuze enhanced juices, teas, waters and energy drinks. The Company expects performance in North America to be weak during 2007.

In North Asia, Eurasia and Middle East, unit case volume grew 11 percent in 2006 compared to 2005, led by double-digit growth in China, Russia and Turkey, partially offset by a 3 percent decline in Japan. The increase in unit case volume in China was led by significant growth in both sparkling and still beverages. The unit case volume growth in Russia and Turkey was the result of improving macroeconomic trends, strong bottler execution and successful marketing programs. Unit case volume in Russia also benefited from the full-year impact of the joint acquisition of Multon, compared to a partial year in 2005. The Company and Coca-Cola HBC jointly acquired Multon, a Russian juice company, in April 2005. The decrease in unit case volume in Japan was primarily due to weakness across core brands including Trademark Coca-Cola, Georgia Coffee and our green tea brands. However, results in Japan gradually improved during 2006 and position Japan for growth in 2007.

Unit case volume for Bottling Investments increased 16 percent in 2006 versus 2005, primarily due to the acquisition of Kerry Beverages Limited, which was subsequently renamed Coca-Cola China Industries Limited (“CCCIL”), and the acquisitions of TJC Holdings (Pty) Ltd., a South African bottling company (“TJC”), and Apollinaris. The Company intends to sell a portion of its investment in TJC to Black Economic Empowerment entities at a future date. Unit case volume for Bottling Investments also increased due to the consolidation of Brucephil, Inc. (“Brucephil”), the parent company of The Philadelphia Coca-Cola Bottling Company. In the third quarter of 2006, our Company signed agreements with J. Bruce Llewellyn and Brucephil for the potential purchase of the remaining shares of Brucephil not currently owned by the Company. The agreements provide for the Company’s purchase of the shares upon the election of Mr. Llewellyn or the election of the Company. Based on the terms of these agreements, the Company concluded that it must consolidate Brucephil under Interpretation No. 46(R). Brucephil’s financial statements were consolidated effective September 29, 2006. The acquisition of the German bottling company Bremer Erfrischungsgetraenke GmbH (“Bremer”) during the third quarter of 2005 also contributed to unit case volume increases in 2006, reflecting the impact of full-year unit case volume in 2006 for Bremer compared to a partial year in 2005. The unit case volume increase was partially offset by a decline in India.

In Africa, unit case volume increased 6 percent in 2005 compared to 2004. This increase was driven by growth in core sparkling beverages as well as still beverages across all divisions in this operating segment.

In East, South Asia and Pacific Rim, unit case volume decreased 4 percent in 2005 compared to 2004, primarily due to declines in India and the Philippines. The decline in India was related to the impact of price increases to cover rising raw material and distribution costs and the lingering effects of the 2003 pesticide allegations. The decline in the Philippines was primarily related to affordability and availability issues.

Unit case volume in the European Union was even in 2005 versus 2004, primarily due to strong growth in Spain and Central Europe partially offset by declines primarily in Germany and Northwest Europe. Unit case volume in Germany declined 2 percent in 2005 due to the continued impact of the mandatory deposit legislation on the availability of nonrefillable packages and the corresponding limited availability of our products in the discount retail channel, along with overall industry weakness. In the second half of 2005, the Company achieved availability of a limited range of its products in most discounters. Results in Germany stabilized in the second half of 2005. Unit case volume in Northwest Europe declined 3 percent in 2005, primarily due to the soft economic environment and declines in sparkling beverages, which was associated with a decrease in competitors’ prices at retailers, and the discount channel becoming a larger part of the retail market, together with a shift in consumer preferences away from regular sparkling beverages driven by health and wellness trends and the associated public opinion, media and government attention.

Unit case volume for Latin America increased 6 percent in 2005 versus 2004, reflecting strong growth in Brazil, Argentina and Mexico, primarily due to growth in sparkling beverages. The increase in Brazil and Mexico was primarily due to strong marketing, execution and package innovation.

In North America, unit case volume in Retail increased 2 percent in 2005 versus 2004, reflecting improved performance in the bottler-delivered business primarily related to Dasani, Coca-Cola Zero and still beverages, along with growth in the warehouse juice and warehouse water operations. Foodservice and Hospitality had a 1 percent increase in 2005 compared to 2004, reflecting improved trends in restaurant traffic and the impact of a new customer conversion partially offset by the impact of higher fuel costs and Hurricane Katrina on consumer restaurant spending.

In North Asia, Eurasia and Middle East, unit case volume grew 15 percent in 2005 versus 2004, led by 22 percent growth in China, 2 percent growth in Japan, 54 percent growth in Russia and 14 percent growth in Turkey. The increase in unit case volume in China was led by significant growth in both sparkling and still beverages. Japan's growth was primarily due to new product introductions. The unit case volume growth in Turkey was largely due to improving macroeconomic trends, strong bottler execution and successful marketing programs. The unit case volume growth in Russia was the result of the joint acquisition of Multon as well as improving macroeconomic trends, strong bottler execution and successful marketing programs.

Unit case volume for Bottling Investments increased 6 percent in 2005 versus 2004, primarily related to the acquisitions and full-year impact of consolidation of certain bottling operations under Interpretation No. 46(R). The unit case volume increase in 2005 was partially offset by a decline in India bottling operations and dispositions of certain bottling operations.

#### *Gallon Sales*

Company-wide gallon sales and unit case volume both grew 4 percent in 2006 when compared to 2005. In Africa, the gallon sales increase was lower than the unit case volume increase mostly due to planned inventory reductions in Nigeria. In East, South Asia and Pacific Rim, the gallon sales decline was lower than the unit case volume decline due to demand for Coca-Cola Zero in Australia and timing of gallon sales in India. In the European Union, unit case volume increased ahead of gallon sales volume due to timing of gallon sales. Both in Latin America and North America, gallon sales and unit case volume were approximately equal. In North Asia, Eurasia and Middle East, unit case volume increased ahead of gallon sales primarily due to inventory reductions in Russia. Unit case volume growth also reflected the impact of a full-year of unit case volume compared to a partial year in 2005 due to the joint acquisition of Multon with Coca-Cola HBC in the second quarter of 2005. The Company only reports unit case volume related to Multon, as the Company does not sell concentrates or syrups to Multon.

Company-wide gallon sales grew 3 percent while unit case volume grew 4 percent in 2005 compared to 2004. In Africa, gallon sales growth of 7 percent exceeded unit case volume growth of 6 percent in 2005 compared to 2004, primarily due to timing of gallon shipments. In East, South Asia and Pacific Rim, the gallon sales decline was higher than the unit case volume decline primarily due to timing of gallon sales in India and the impact of 2005 planned inventory reductions in Australia. Both in the European Union and in Latin America, gallon sales growth and unit case volume growth were even in 2005 versus 2004. In North America, gallon sales increased 1 percent while unit case volume increased 2 percent, primarily due to the impact of higher gallon sales in 2004 related to the launch of Coca-Cola C2 and a change in shipping routes in 2004. In North Asia, Eurasia and Middle East, unit case volume increased ahead of gallon sales volume due to the joint acquisition of Multon, which contributed to unit case volume in 2005, along with timing of 2004 gallon sales, which impacted most of the remaining divisions in the operating segment. Multon had full-year unit case volume of approximately 80 million unit cases in 2004.

*Analysis of Consolidated Statements of Income*

Year Ended December 31, (In millions except per share data and percentages)	2006	2005	2004	Percent Change	
				2006 vs. 2005	2005 vs. 2004
<b>NET OPERATING REVENUES</b>	<b>\$ 24,088</b>	\$ 23,104	\$ 21,742	4%	6%
Cost of goods sold	<b>8,164</b>	8,195	7,674	0	7
<b>GROSS PROFIT</b>	<b>15,924</b>	14,909	14,068	7	6
<b>GROSS PROFIT MARGIN</b>	<b>66.1%</b>	64.5%	64.7%		
Selling, general and administrative expenses	<b>9,431</b>	8,739	7,890	8	11
Other operating charges	<b>185</b>	85	480	*	*
<b>OPERATING INCOME</b>	<b>6,308</b>	6,085	5,698	4	7
<b>OPERATING MARGIN</b>	<b>26.2%</b>	26.3%	26.2%		
Interest income	<b>193</b>	235	157	(18)	50
Interest expense	<b>220</b>	240	196	(8)	22
Equity income — net	<b>102</b>	680	621	(85)	10
Other income (loss) — net	<b>195</b>	(93)	(82)	*	*
Gains on issuances of stock by equity investees	<b>—</b>	23	24	*	*
<b>INCOME BEFORE INCOME TAXES</b>	<b>6,578</b>	6,690	6,222	(2)	8
Income taxes	<b>1,498</b>	1,818	1,375	(18)	32
Effective tax rate	<b>22.8%</b>	27.2%	22.1%		
<b>NET INCOME</b>	<b>\$ 5,080</b>	\$ 4,872	\$ 4,847	4%	1%
<b>PERCENTAGE OF NET OPERATING REVENUES</b>	<b>21.1%</b>	21.1%	22.3%		
<b>NET INCOME PER SHARE:</b>					
Basic	<b>\$ 2.16</b>	\$ 2.04	\$ 2.00	6%	2%
Diluted	<b>\$ 2.16</b>	\$ 2.04	\$ 2.00	6%	2%

\* Calculation is not meaningful.

### *Net Operating Revenues*

Net operating revenues increased by \$984 million or 4 percent in 2006 versus 2005. Net operating revenues increased by \$1,362 million or 6 percent in 2005 versus 2004.

The following table indicates, on a percentage basis, the estimated impact of key factors resulting in significant increases (decreases) in net operating revenues:

Year Ended December 31,	Percent Change	
	2006 vs. 2005	2005 vs. 2004
Increase in gallon sales	4%	3%
Structural changes	(2)	0
Price and product/geographic mix	2	1
Impact of currency fluctuations versus the U.S. dollar	0	2
Total percentage increase	4%	6%

Refer to the heading “Volume” for a detailed discussion on gallon sales.

“Structural changes” refers to acquisitions or dispositions of bottling or canning operations and consolidation or deconsolidation of bottling entities for accounting purposes. In 2006, structural changes decreased net operating revenues by 2 percent compared to 2005, primarily due to the change of the business model in Spain, partially offset by the acquisitions of Bremer in the third quarter of 2005, TJC in the first quarter of 2006, CCCIL in the third quarter of 2006 and the consolidation of Brucephil under Interpretation No. 46(R) effective September 29, 2006. Refer to Note 19 of Notes to Consolidated Financial Statements. Effective January 1, 2006, the Company granted our bottling partners in Spain the rights to manufacture and distribute Company trademarked products in can packages. Prior to granting these rights to our bottling partners, the Company held the manufacturing and distribution rights for these can packages in Spain. In connection with granting these rights, the Company reduced our planned future annual marketing support payments to our bottling partners in Spain. These changes resulted in a reduction of net operating revenues and cost of goods sold. This change did not materially impact gross profit for 2006. If the change had occurred as of January 1, 2005, net operating revenues for 2005 would have been reduced by approximately \$779 million.

Price and product/geographic mix increased net operating revenues by 2 percent in 2006 compared to 2005, primarily due to price increases across the majority of the operating segments and improved pricing and product/package mix in Bottling Investments partially offset by unfavorable product mix primarily in Japan.

In 2005, structural changes reflect the impact of a full year of revenue in 2005 for variable interest entities compared to a partial year in 2004. Under Interpretation No. 46(R), the results of operations of variable interest entities in which the Company was determined to be the primary beneficiary were included in our consolidated results beginning April 2, 2004. Refer to Note 1 of Notes to Consolidated Financial Statements. The acquisition of Bremer during the third quarter of 2005 also favorably impacted net operating revenues. Refer to Note 19 of Notes to Consolidated Financial Statements. These increases in net operating revenues were offset by the dispositions of certain bottling and canning operations which were not material individually or in aggregate.

The favorable impact of foreign currency fluctuations in 2005 versus 2004 resulted from the strength of most key foreign currencies versus the U.S. dollar, especially a stronger euro, which favorably impacted the European Union and Bottling Investments, and a stronger Brazilian real and Mexican peso, that favorably impacted Latin America and Bottling Investments. The favorable impact of fluctuation in these currencies was partially offset by a weaker Japanese yen, which unfavorably impacted North Asia, Eurasia and Middle East. Refer to the heading “Liquidity, Capital Resources and Financial Position—Foreign Exchange.”

Price and product/geographic mix increased net operating revenues by 1 percent in 2005 compared to 2004, primarily due to price increases across the majority of the operating segments and improved product/package mix in Bottling Investments, partially offset by unfavorable country mix.

Information about our net operating revenues by operating segment as a percentage of Company net operating revenues is as follows:

Year Ended December 31,	2006	2005	2004
Africa	4.6%	4.8%	4.4%
East, South Asia and Pacific Rim	3.3	3.1	3.2
European Union	14.6	17.8	18.0
Latin America	10.3	8.9	8.2
North America	29.1	28.9	29.5
North Asia, Eurasia and Middle East	16.5	17.7	17.9
Bottling Investments	21.2	18.4	18.3
Corporate	0.4	0.4	0.5
	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>

The percentage contribution of each operating segment has changed due to net operating revenues in certain segments growing at a faster rate compared to the other operating segments, the impact of foreign currency fluctuations; and the acquisitions of CCCIL and TJC, and the consolidation of Brucephil under Interpretation No. 46(R), which impacted Bottling Investments. The acquisition of Bremer during the third quarter of 2005 also increased net operating revenues in 2006, reflecting the impact of full-year net operating revenues in 2006 for Bremer compared to a partial year in 2005.

The size and timing of structural changes, including acquisitions or dispositions of bottling and canning operations, do not occur consistently from period to period. As a result, anticipating the impact of such events on future increases or decreases in net operating revenues (and other financial statement line items) usually is not possible. However, we expect to continue to buy and sell bottling interests in limited circumstances and, as a result, structural changes will continue to affect our consolidated financial statements in future periods.

### ***Gross Profit***

Our gross profit margin increased to 66.1 percent in 2006 from 64.5 percent in 2005. Our gross margin was favorably impacted by the change in the business model in Spain, as discussed above. Other structural changes, which included the consolidation of Brucephil under Interpretation No. 46(R) in 2006, the acquisitions of CCCIL and TJC in 2006, and the acquisition of Bremer in 2005, unfavorably impacted our gross profit margin. Generally, bottling and finished product operations produce higher net operating revenues but lower gross profit margins compared to concentrate and syrup operations. Our gross margin in 2006 was also impacted favorably by price increases, partially offset by increases in the cost of raw materials and freight, primarily in North America, and by an unfavorable product mix, primarily in Japan. Gross profit margin in 2005 was favorably impacted by the receipt of approximately \$109 million in proceeds related to a class action lawsuit settlement concerning price-fixing in the sale of high fructose corn syrup (“HFCS”) purchased by the Company during the years 1991 to 1995. Subsequent to the receipt of this settlement, the Company distributed approximately \$62 million to certain bottlers in North America. From 1991 to 1995, the Company purchased HFCS on behalf of those bottlers. Therefore, those bottlers ultimately were entitled to a portion of the proceeds. The Company’s portion of the settlement was approximately \$47 million, which was recorded as a reduction of cost of goods sold and impacted Corporate. Refer to Note 18 of Notes to Consolidated Financial Statements.

In 2007, the Company expects the cost of raw materials to increase, primarily in North America. We will attempt to mitigate the overall impact on our business through appropriate pricing and other strategies.

Our gross profit margin decreased to 64.5 percent in 2005 from 64.7 percent in 2004, primarily due to higher raw material and freight costs driven by rising oil prices. This decrease was partially offset by the receipt of net settlement proceeds of approximately \$47 million, as discussed above. Our gross margin was also impacted by the consolidation of certain bottling operations under Interpretation No. 46(R) as of April 2, 2004. Refer to Note 1 of Notes to Consolidated Financial Statements.

### *Selling, General and Administrative Expenses*

The following table sets forth the significant components of selling, general and administrative expenses (in millions):

Year Ended December 31,	2006	2005	2004
Selling expenses	\$ 3,924	\$ 3,453	\$ 3,031
Advertising expenses	2,553	2,475	2,165
General and administrative expenses	2,630	2,487	2,349
Stock-based compensation expense	324	324	345
Selling, general and administrative expenses	\$ 9,431	\$ 8,739	\$ 7,890

Total selling, general and administrative expenses were approximately 8 percent higher in 2006 versus 2005. The increases in selling and advertising expenses were primarily related to increased investments in marketing activities, including World Cup and Winter Olympics promotions in the European Union, combined with new product innovation activities and increased costs in our consolidated bottling investments as a result of acquisitions and consolidation of certain bottling operations. General and administrative expenses increased due to higher costs in Bottling Investments related to the acquisitions of CCCIL and TJC and the consolidation of Brucephil under Interpretation No. 46(R). The acquisition of Bremer during the third quarter of 2005 also increased general and administrative expenses in 2006, reflecting a full-year impact in 2006 for Bremer compared to a partial year in 2005. General and administrative expenses in 2006 also reflected the impact of a \$100 million donation made to The Coca-Cola Foundation, which impacted Corporate. Stock-based compensation expense was flat in 2006 compared to 2005. Stock-based compensation expense in 2005 included approximately \$50 million of expense due to a change in our estimated service period for retirement-eligible participants in our plans. This amount was offset primarily by the impact of the timing of stock-based compensation grants in prior years.

As of December 31, 2006, we had approximately \$376 million of total unrecognized compensation cost related to nonvested share-based compensation arrangements granted under our plans. This cost is expected to be recognized as stock-based compensation expense over a weighted-average period of 1.7 years. This expected cost does not include the impact of any future stock-based compensation awards. Refer to Note 15 of Notes to Consolidated Financial Statements.

Total selling, general and administrative expenses were approximately 11 percent higher in 2005 versus 2004. Approximately 1 percentage point of this increase was due to an overall weaker U.S. dollar (especially compared to the Brazilian real, the Mexican peso and the euro). The increase in selling, advertising and general and administrative expenses was primarily related to increased marketing and innovation expenses and the full-year impact of the consolidation of certain bottling operations under Interpretation No. 46(R). The decrease in stock-based compensation expense was primarily related to the lower average fair value per share of stock options expensed in 2005 compared to the average fair value per share expensed in 2004. This decrease was partially offset by approximately \$50 million of accelerated amortization of compensation expense related to a change in our estimated service period for retirement-eligible participants when the terms of their stock-based compensation awards provided for accelerated vesting upon early retirement. Refer to Note 15 of Notes to Consolidated Financial Statements.

### *Other Operating Charges*

The other operating charges incurred by operating segment were as follows (in millions):

Year Ended December 31,	2006	2005	2004
Africa	\$ 3	\$ —	\$ —
East, South Asia and Pacific Rim	44	85	—
European Union	36	—	—
Latin America	—	—	—
North America	—	—	18
North Asia, Eurasia and Middle East	17	—	—
Bottling Investments	84	—	398
Corporate	1	—	64
Total	\$ 185	\$ 85	\$ 480

During 2006, our Company recorded other operating charges of \$185 million. Of these charges, approximately \$108 million were primarily related to the impairment of assets and investments in our bottling operations, approximately \$53 million were for contract termination costs related to production capacity efficiencies and approximately \$24 million were related to other restructuring costs. None of these charges was individually significant. The impairment charges were primarily the result of a revised outlook for certain assets and bottling operations in Asia, which have been impacted by unfavorable market conditions and declines in volume. Refer to the discussion under “Critical Accounting Policies and Estimates—Goodwill, Trademarks and Other Intangible Assets,” above.

Other operating charges in 2005 reflected the impact of approximately \$84 million of expenses related to impairment charges for intangible assets and approximately \$1 million related to impairments of other assets. These intangible assets primarily relate to trademark beverages sold in the Philippines, which is part of East, South Asia and Pacific Rim. Refer to the heading “Critical Accounting Policies and Estimates—Goodwill, Trademarks and Other Intangible Assets.”

Other operating charges in 2004 reflected the impact of approximately \$480 million of expenses primarily related to impairment charges for franchise rights and certain manufacturing assets. Bottling Investments accounted for approximately \$398 million of the impairment charges, which were primarily related to the impairment of franchise rights at CCEAG. For a discussion of the operating environment in Germany, refer to the heading “Critical Accounting Policies and Estimates—Goodwill, Trademarks and Other Intangible Assets.” Corporate accounted for approximately \$64 million of impairment charges, which were primarily related to the impairment of certain manufacturing assets.

### *Operating Income and Operating Margin*

Information about our operating income contribution by operating segment on a percentage basis is as follows:

Year Ended December 31,	2006	2005	2004
Africa	6.7%	6.5%	5.9%
East, South Asia and Pacific Rim	5.7	4.6	7.7
European Union	35.7	36.5	37.3
Latin America	23.0	19.3	18.5
North America	26.7	25.5	28.2
North Asia, Eurasia and Middle East	24.7	29.0	29.3
Bottling Investments	—	(1.0)	(8.0)
Corporate	(22.5)	(20.4)	(18.9)
	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>

Information about our operating margin on a consolidated basis and by operating segment is as follows:

Year Ended December 31,	2006	2005	2004
Consolidated	26.2%	26.3%	26.2%
Africa	38.4%	35.8%	35.0%
East, South Asia and Pacific Rim	45.0	39.5	62.2
European Union	64.3	54.1	54.3
Latin America	57.9	57.0	59.2
North America	24.0	23.3	25.0
North Asia, Eurasia and Middle East	39.1	42.4	43.0
Bottling Investments	—	(1.0)	(11.4)
Corporate	*	*	*

\* Calculation is not meaningful.

As demonstrated by the tables above, the percentage contribution to operating income and operating margin by each operating segment fluctuated from year to year. Operating income and operating margin by operating segment were influenced by a variety of factors and events including the following:

- In 2006, foreign currency exchange rates unfavorably impacted operating income by approximately 1 percent, primarily related to a weaker Japanese yen, which impacted North Asia, Eurasia and Middle East. The unfavorable impact from the weaker Japanese yen was partially offset by favorable foreign currency exchange rate changes primarily related to the euro, which impacted the European Union and Bottling Investments, and the Brazilian real, which impacted Latin America and Bottling Investments.
- In 2006, price increases across the majority of operating segments favorably impacted both operating income and operating margins.
- In 2006, increased spending on marketing and innovation activities impacted the majority of the operating segments' operating income and operating margins. Refer to the heading "Selling, General and Administrative Expenses."
- In 2006, operating income was reduced by approximately \$3 million for Africa, \$44 million for East, South Asia and Pacific Rim, \$36 million for the European Union, \$17 million for North Asia, Eurasia and Middle East, \$88 million for Bottling Investments and \$1 million for Corporate primarily due to contract termination costs related to production capacity efficiencies, asset impairments and other restructuring costs. Refer to Note 20 of Notes to Consolidated Financial Statements.

- In 2006, the increase in operating margin for the European Union was primarily due to a change in the business model in Spain. Refer to the headings “Net Operating Revenues” and “Gross Profit,” above.
- In 2006, the decrease in operating income and operating margin for North Asia, Eurasia and Middle East was primarily due to unfavorable product mix in Japan, which was partially offset by increased operating income in Russia and Turkey. Operating margins in Japan are higher than the operating margins in Russia and Turkey.
- In 2006, the increase in operating income and operating margin for Bottling Investments was primarily due to price increases, favorable package mix and actions to improve efficiency.
- In 2006, operating income was reduced by \$100 million for Corporate as a result of a donation made to The Coca-Cola Foundation.
- In 2005, operating income increased approximately 7 percent. Of this amount, 4 percent was due to favorable foreign currency exchange primarily related to the Brazilian real and the Mexican peso, which impacted Latin America and Bottling Investments, and the euro, which impacted the European Union and Bottling Investments.
- In 2005, operating income was impacted by an increase in net operating revenues and gross profit, partially offset by increased spending on marketing and innovation activities in each operating segment. Refer to the headings “Net Operating Revenues” and “Selling, General and Administrative Expenses.”
- In 2005, as a result of impairment charges totaling approximately \$85 million related to the Philippines, operating margins in the East, South Asia and Pacific Rim operating segment decreased. Refer to the heading “Other Operating Charges.”
- In 2005, operating income in Corporate decreased \$146 million, primarily due to increased marketing and innovation expenses, which were partially offset by our receipt of a net settlement of approximately \$47 million related to a class action lawsuit concerning the purchase of HFCS. Refer to the headings “Gross Profit” and “Selling, General and Administrative Expenses.”
- In 2004, operating income was reduced by approximately \$18 million for North America, \$398 million for Bottling Investments and \$64 million for Corporate as a result of impairment charges. Refer to the heading “Other Operating Charges.”
- In 2004, operating income increased approximately 9 percent. Of this amount, 8 percent was due to favorable foreign currency exchange primarily related to the euro, which impacted the European Union, and the Japanese yen, which impacted North Asia, Eurasia and Middle East.
- In 2004, as a result of the creation of a nationally integrated supply chain management company in Japan, operating margins in North Asia, Eurasia and Middle East increased. Effective October 1, 2003, the Company and all of our bottling partners in Japan created a nationally integrated supply chain management company to centralize procurement, production and logistics operations for the entire Coca-Cola system in Japan. As a result, a portion of our Company’s business was essentially converted from a finished product business model to a concentrate business model. This shift of certain products to a concentrate business model resulted in reductions in our revenues and cost of goods sold, each in the same amount. This change in the business model did not impact gross profit. Generally, concentrate and syrup operations produce lower net revenues but higher operating margins compared to finished product operations.
- In 2004, as a result of the consolidation of certain bottling operations that are considered variable interest entities under Interpretation No. 46(R), operating margin for Bottling Investments was reduced. Generally, bottling operations produce higher net revenues but lower operating margins compared to concentrate and syrup operations.

- In 2004, operating income in Corporate increased \$75 million due to the receipt of an insurance settlement related to the class action lawsuit which was settled in 2000.
- In 2004, operating income in Corporate decreased \$75 million due to a donation to The Coca-Cola Foundation.

### *Interest Income and Interest Expense*

We monitor our mix of fixed-rate and variable-rate debt as well as our mix of short-term debt versus long-term debt. From time to time we enter into interest rate swap agreements to manage our mix of fixed-rate and variable-rate debt.

In 2006, interest income decreased by \$42 million compared to 2005, primarily due to lower average short-term investment balances, partially offset by higher average interest rates. Interest expense in 2006 decreased by \$20 million compared to 2005. This decrease is primarily the result of lower average balances on commercial paper borrowings, partially offset by higher average interest rates. We expect 2007 net interest expense to increase due to forecasted lower cash balances and higher debt balances.

In 2005, interest income increased by \$78 million compared to 2004, primarily due to higher average short-term investment balances and higher average interest rates on U.S. dollar denominated deposits. Interest expense in 2005 increased by \$44 million compared to 2004, primarily due to higher average interest rates on commercial paper borrowings in the United States, partially offset by lower interest expense at CCEAG due to the repayment of current maturities of long-term debt in 2005.

### *Equity Income—Net*

Our Company's share of income from equity method investments for 2006 totaled \$102 million, compared to \$680 million in 2005, a decrease of \$578 million. Equity income in 2006 was reduced by approximately \$602 million resulting from the impact of our proportionate share of an impairment charge recorded by CCE. CCE recorded a \$2.9 billion pretax (\$1.8 billion after tax) impairment of its North American franchise rights. The decline in the estimated fair value of CCE's North American franchise rights was the result of several factors, including but not limited to (1) CCE's revised outlook on 2007 raw material costs driven by significant increases in aluminum and HFCS; (2) a challenging marketplace environment with increased pricing pressures in several high-growth beverage categories; and (3) increased interest rates contributing to a higher discount rate and corresponding capital charge. Our 2006 equity income—net also reflected a net decrease of approximately \$37 million primarily related to other impairment and restructuring charges recorded by CCE and certain other equity method investees, partially offset by approximately \$33 million related to our proportionate share of favorable changes in certain of CCE's state and Canadian federal and provincial tax rates. In addition, our 2006 equity income was slightly impacted by the Company's sale of shares representing 8 percent of the capital stock of Coca-Cola FEMSA. The Company sold these shares to Fomento Economico Mexicano, S.A.B. de C.V. ("FEMSA"), the major shareowner of Coca-Cola FEMSA, in November 2006. As a result of this sale, our ownership interest in Coca-Cola FEMSA was reduced from approximately 40 percent to approximately 32 percent. The decrease in 2006 equity income was also the result of the sale of a portion of our investment in Coca-Cola Icecek A.S. ("Coca-Cola Icecek") in an initial public offering during the second quarter of 2006. As a result of this public offering, our Company's interest in Coca-Cola Icecek decreased from approximately 36 percent to approximately 20 percent. These reductions in ownership of Coca-Cola FEMSA and Coca-Cola Icecek will reduce our future equity income related to these equity method investees. Refer to Note 3 of Notes to Consolidated Financial Statements. The decrease in equity income for 2006 was partially offset by our Company's proportionate share of increased net income from certain of the equity method investees and our proportionate share of the net income of the Multon juice joint venture in Russia.

In February 2007, CCE announced that it would restructure segments of its Corporate, North America and European operations. As a part of the restructuring, CCE expects a net job reduction of approximately 3,500

positions, or 5 percent of its total workforce. CCE expects this restructuring will result in a charge of approximately \$300 million, with the majority to be recognized in 2007 and 2008. The Company's equity income in 2007 and 2008 will reflect our proportionate share of the restructuring charges recorded by CCE.

Our Company's share of income from equity method investments for 2005 totaled \$680 million compared to \$621 million in 2004, an increase of \$59 million or 10 percent, primarily due to the overall improving health of the Coca-Cola bottling system in most of the world and the joint acquisition of Multon in April 2005. The increase was offset by approximately \$33 million related to our proportionate share of certain charges recorded by CCE. These charges included approximately \$51 million, primarily related to the tax liability resulting from the repatriation of previously unremitted foreign earnings under the Jobs Creation Act, and approximately \$18 million due to restructuring charges recorded by CCE. These charges were offset by approximately \$37 million from CCE's HFCS lawsuit settlement and changes in certain of CCE's state and provincial tax rates.

#### ***Other Income (Loss)—Net***

Other income (loss)—net was a net income of \$195 million for 2006 compared to a net loss of \$93 million for 2005, a difference of \$288 million. In 2006, other income (loss)—net included a gain of approximately \$175 million resulting from the sale of a portion of our Coca-Cola FEMSA shares to FEMSA and a gain of approximately \$123 million resulting from the sale of a portion of our investment in Coca-Cola Icecek shares in an initial public offering. Refer to Note 18 of Notes to Consolidated Financial Statements. This line item in 2006 also included \$15 million in foreign currency exchange losses, the accretion of \$58 million for the discounted value of our liability to purchase CCEAG shares (refer to Note 8 of Notes to Consolidated Financial Statements) and the minority shareowners' proportional share of net income of certain consolidated subsidiaries.

Other income (loss)—net amounted to a net loss of \$93 million for 2005 compared to a net loss of \$82 million for 2004, a difference of \$11 million. The difference was primarily related to a reduction in foreign exchange losses. This line item in 2005 primarily consisted of \$23 million in foreign currency exchange losses, the accretion of \$60 million for the discounted value of our liability to purchase CCEAG shares (refer to Note 8 of Notes to Consolidated Financial Statements) and the minority shareowners' proportional share of net income of certain consolidated subsidiaries.

#### ***Gains on Issuances of Stock by Equity Method Investees***

When one of our equity method investees issues additional shares to third parties, our percentage ownership interest in the investee decreases. In the event the issuance price per share is higher or lower than our average carrying amount per share, we recognize a noncash gain or loss on the issuance, when appropriate. This noncash gain or loss, net of any deferred taxes, is recognized in our net income in the period the change of ownership interest occurs.

In 2006, our equity method investees did not issue any additional shares to third parties that resulted in our Company recording any noncash pretax gains.

In 2005, our Company recorded approximately \$23 million of noncash pretax gains on the issuances of stock by equity method investees. The issuances primarily related to Coca-Cola Amatil's issuance of common stock in connection with the acquisition of SPC Ardmona Pty. Ltd., an Australian packaged fruit company. These issuances of common stock reduced our ownership interest in the total outstanding shares of Coca-Cola Amatil from approximately 34 percent to approximately 32 percent.

In 2004, our Company recorded approximately \$24 million of noncash pretax gains on issuances of stock by CCE. The issuances primarily related to the exercise of CCE stock options by CCE employees at amounts greater than the book value per share of our investment in CCE. These issuances of stock reduced our

ownership interest in the total outstanding shares of CCE common stock from approximately 37 percent to approximately 36 percent.

### *Income Taxes*

Our effective tax rate reflects tax benefits derived from significant operations outside the United States, which are generally taxed at rates lower than the U.S. statutory rate of 35 percent.

Our effective tax rate of approximately 22.8 percent for the year ended December 31, 2006, included the following:

- a tax benefit of approximately 1.8 percent primarily related to the sale of a portion of our investments in Coca-Cola Icecek and Coca-Cola FEMSA. The tax benefit was a result of the reversal of a valuation allowance that covered certain deferred tax assets recorded on capital loss carryforwards. The reversal of the valuation allowance was offset by a reduction of deferred tax assets due to the utilization of these capital loss carryforwards. These capital loss carryforwards offset the taxable gain on the sale of a portion of our investments in Coca-Cola Icecek and Coca-Cola FEMSA. Also included in this tax benefit is the reversal of the deferred tax liability recorded for the differences between the financial reporting and tax bases in the stock sold;
- an income tax benefit primarily related to the impairment of assets and investments in our bottling operations, contract termination costs related to production capacity efficiencies and other restructuring charges at a rate of approximately 16 percent;
- a tax charge of approximately \$24 million related to the resolution of certain tax matters; and
- an income tax benefit related to our proportionate share of CCE's charges recorded at a rate of approximately 8.8 percent. Refer to Note 3 and Note 18 of Notes to Consolidated Financial Statements.

Our effective tax rate of approximately 27.2 percent for the year ended December 31, 2005, included the following:

- an income tax benefit primarily related to the Philippines impairment charges at a rate of approximately 4 percent;
- an income tax benefit of approximately \$101 million related to the reversal of previously accrued taxes resulting from the favorable resolution of various tax matters; and
- a tax provision of approximately \$315 million related to repatriation of previously unremitted foreign earnings under the Jobs Creation Act.

Our effective tax rate of approximately 22.1 percent for the year ended December 31, 2004, included the following:

- an income tax benefit of approximately \$128 million related to the reversal of previously accrued taxes resulting from the favorable resolution of various tax matters;
- an income tax benefit on "Other Operating Charges," discussed above, at a rate of approximately 36 percent;
- an income tax provision of approximately \$75 million related to the recording of a valuation allowance on deferred tax assets of CCEAG; and
- an income tax benefit of approximately \$50 million as a result of the realization of certain tax credits related to the Jobs Creation Act.

Based on current tax laws, the Company's effective tax rate in 2007 is expected to be approximately 23 percent before considering the effect of any unusual or special items that may affect our tax rate in future years.

## Liquidity, Capital Resources and Financial Position

We believe our ability to generate cash from operating activities is one of our fundamental financial strengths. We expect cash flows from operating activities to be strong in 2007 and in future years. Accordingly, our Company expects to meet all of our financial commitments and operating needs for the foreseeable future. We expect to use cash generated from operating activities primarily for dividends, share repurchases, acquisitions and aggregate contractual obligations.

### *Cash Flows from Operating Activities*

Net cash provided by operating activities for the years ended December 31, 2006, 2005 and 2004 was approximately \$6.0 billion, \$6.4 billion and \$6.0 billion, respectively.

Cash flows from operating activities decreased 7 percent in 2006 compared to 2005. This decrease was primarily the result of payments in 2006 of marketing accruals recorded in 2005 related to increased marketing and innovation activities and increased tax payments made in the first quarter of 2006 related to the 2005 repatriation of foreign earnings under the Jobs Creation Act. This decrease was partially offset by an increase in cash receipts in 2006 from customers, which was driven by a 4 percent growth in net operating revenues. Our cash flows from operating activities in 2006 also decreased versus 2005 as a result of a contribution of approximately \$216 million to a U.S. Voluntary Employee Beneficiary Association ("VEBA"), a tax-qualified trust to fund retiree medical benefits (refer to Note 16 of Notes to Consolidated Financial Statements) and a \$100 million donation made to The Coca-Cola Foundation.

Cash flows from operating activities increased 8 percent in 2005 compared to 2004. The increase was primarily related to an increase in cash receipts from customers, which was driven by a 6 percent growth in net operating revenues. These higher cash collections were offset by increased payments to suppliers and vendors, including payments related to our increased marketing spending. Our cash flows from operating activities in 2005 also improved versus 2004 as a result of a \$137 million reduction in payments related to our 2003 streamlining initiatives. Cash flows from operating activities in 2005 were unfavorably impacted by a \$176 million increase in income tax payments primarily related to payment of a portion of the tax provision associated with the repatriation of previously unremitted foreign earnings under the Jobs Creation Act.

### *Cash Flows from Investing Activities*

Our cash flows used in investing activities are summarized as follows (in millions):

Year Ended December 31,	2006	2005	2004
Cash flows (used in) provided by investing activities:			
Acquisitions and investments, principally trademarks and bottling companies	\$ (901)	\$ (637)	\$ (267)
Purchases of other investments	(82)	(53)	(46)
Proceeds from disposals of other investments	640	33	161
Purchases of property, plant and equipment	(1,407)	(899)	(755)
Proceeds from disposals of property, plant and equipment	112	88	341
Other investing activities	(62)	(28)	63
Net cash used in investing activities	\$ (1,700)	\$ (1,496)	\$ (503)

Purchases of property, plant and equipment accounted for the most significant cash outlays for investing activities in each of the three years ended December 31, 2006. Our Company currently estimates that purchases of property, plant and equipment in 2007 will be approximately \$1.5 billion.

Total capital expenditures for property, plant and equipment (including our investments in information technology) and the percentage of such totals by operating segment for 2006, 2005 and 2004 were as follows:

Year Ended December 31,	2006	2005	2004
Capital expenditures (in millions)	<b>\$ 1,407</b>	\$ 899	\$ 755
Africa	<b>2.7%</b>	2.5%	2.3%
East, South Asia and Pacific Rim	<b>0.7</b>	0.8	0.9
European Union	<b>6.6</b>	8.6	5.1
Latin America	<b>3.1</b>	2.7	3.4
North America	<b>29.9</b>	29.5	32.7
North Asia, Eurasia and Middle East	<b>9.2</b>	9.9	6.0
Bottling Investments	<b>29.7</b>	29.4	34.1
Corporate	<b>18.1</b>	16.6	15.5

Acquisitions and investments represented the next most significant investing activity, accounting for \$901 million in 2006, \$637 million in 2005 and \$267 million in 2004.

In 2006, our Company acquired a controlling interest in CCCIL and acquired Apollinaris and TJC. Refer to Note 19 of Notes to Consolidated Financial Statements. The remaining amount of cash used for acquisitions and investments was primarily related to the acquisition of various trademarks and brands, none of which were individually significant.

Investing activities in 2006 also included proceeds of approximately \$198 million received from the sale of shares in connection with the initial public offering of Coca-Cola Icecek and proceeds of approximately \$427 million received from the sale of a portion of Coca-Cola FEMSA shares to FEMSA. Refer to Note 3 of Notes to Consolidated Financial Statements.

In April 2005, our Company and Coca-Cola HBC jointly acquired Multon for a total purchase price of approximately \$501 million, split equally between the Company and Coca-Cola HBC. During the third quarter of 2005, our Company acquired the German bottling company Bremer for approximately \$160 million from InBev SA. Also in 2005, the Company acquired Sucos Mais, a Brazilian juice company, and completed the acquisition of the remaining 49 percent interest in the business of CCDA Waters L.L.C. not previously owned by our Company. Refer to Note 19 of Notes to Consolidated Financial Statements.

In 2004, proceeds from disposals of property, plant and equipment of approximately \$341 million related primarily to the sale of production assets in Japan. Refer to Note 3 of Notes to Consolidated Financial Statements. In 2004, cash payments for acquisitions and investments were primarily related to the purchase of trademarks in Latin America.

### *Cash Flows from Financing Activities*

Our cash flows used in financing activities were as follows (in millions):

Year Ended December 31,	2006	2005	2004
Cash flows provided by (used in) financing activities:			
Issuances of debt	<b>\$ 617</b>	\$ 178	\$ 3,030
Payments of debt	<b>(2,021)</b>	(2,460)	(1,316)
Issuances of stock	<b>148</b>	230	193
Purchases of stock for treasury	<b>(2,416)</b>	(2,055)	(1,739)
Dividends	<b>(2,911)</b>	(2,678)	(2,429)
Net cash used in financing activities	<b>\$ (6,583)</b>	\$ (6,785)	\$ (2,261)

## *Debt Financing*

Our Company maintains debt levels we consider prudent based on our cash flows, interest coverage ratio and percentage of debt to capital. We use debt financing to lower our overall cost of capital, which increases our return on shareowners' equity.

As of December 31, 2006, our long-term debt was rated "A+" by Standard & Poor's and "Aa3" by Moody's, and our commercial paper program was rated "A-1" and "P-1" by Standard & Poor's and Moody's, respectively. In assessing our credit strength, both Standard & Poor's and Moody's consider our capital structure and financial policies as well as the aggregated balance sheet and other financial information for the Company and certain bottlers, including CCE and Coca-Cola HBC. While the Company has no legal obligation for the debt of these bottlers, the rating agencies believe the strategic importance of the bottlers to the Company's business model provides the Company with an incentive to keep these bottlers viable. If our credit ratings were reduced by the rating agencies, our interest expense could increase. Additionally, if certain bottlers' credit ratings were to decline, the Company's share of equity income could be reduced as a result of the potential increase in interest expense for these bottlers.

We monitor our interest coverage ratio and, as indicated above, the rating agencies consider our ratio in assessing our credit ratings. However, the rating agencies aggregate financial data for certain bottlers along with our Company when assessing our debt rating. As such, the key measure to rating agencies is the aggregate interest coverage ratio of the Company and certain bottlers. Both Standard & Poor's and Moody's employ different aggregation methodologies and have different thresholds for the aggregate interest coverage ratio. These thresholds are not necessarily permanent, nor are they fully disclosed to our Company.

Our global presence and strong capital position give us access to key financial markets around the world, enabling us to raise funds at a low effective cost. This posture, coupled with active management of our mix of short-term and long-term debt and our mix of fixed-rate and variable-rate debt, results in a lower overall cost of borrowing. Our debt management policies, in conjunction with our share repurchase programs and investment activity, can result in current liabilities exceeding current assets.

Issuances and payments of debt included both short-term and long-term financing activities. On December 31, 2006, we had \$1,952 million in lines of credit and other short-term credit facilities available, of which approximately \$225 million was outstanding. The outstanding amount of \$225 million was primarily related to our international operations.

The issuances of debt in 2006 primarily included approximately \$484 million of issuances of commercial paper and short-term debt with maturities of greater than 90 days. The payments of debt in 2006 primarily included approximately \$580 million related to commercial paper and short-term debt with maturities of greater than 90 days and approximately \$1,383 million of net repayments of commercial paper and short-term debt with maturities of 90 days or less.

The issuances of debt in 2005 primarily included approximately \$144 million of issuances of commercial paper with maturities of 90 days or more. The payments of debt primarily included approximately \$1,037 million related to net repayments of commercial paper with maturities of less than 90 days, repayments of commercial paper with maturities greater than 90 days of approximately \$32 million and repayment of approximately \$1,363 million of long-term debt.

The issuances of debt in 2004 primarily included approximately \$2,109 million of net issuances of commercial paper with maturities of 90 days or less, and approximately \$818 million of issuances of commercial paper with maturities of more than 90 days. The payments of debt in 2004 primarily included approximately \$927 million related to commercial paper with maturities of more than 90 days and \$367 million of long-term debt.

### *Share Repurchases*

In October 1996, our Board of Directors authorized a plan (“1996 Plan”) to repurchase up to 206 million shares of our Company’s common stock through 2006. On July 20, 2006, the Board of Directors of the Company authorized a new share repurchase program of up to 300 million shares of the Company’s common stock. The new program took effect upon the expiration of the 1996 Plan on October 31, 2006. The table below presents annual shares repurchased and average price per share:

Year Ended December 31,	2006	2005	2004
Number of shares repurchased (in millions)	55	46	38
Average price per share	\$ 45.19	\$ 43.26	\$ 46.33

Since the inception of our initial share repurchase program in 1984 through our current program as of December 31, 2006, we have purchased more than 1.2 billion shares of our Company’s common stock at an average price per share of \$17.53.

As strong cash flows are expected to continue in the future, the Company currently expects 2007 share repurchases to be in the range of \$2.5 billion to \$3.0 billion.

### *Dividends*

At its February 2007 meeting, our Board of Directors increased our quarterly dividend by 10 percent, raising it to \$0.34 per share, equivalent to a full-year dividend of \$1.36 per share in 2007. This is our 45<sup>th</sup> consecutive annual increase. Our annual common stock dividend was \$1.24 per share, \$1.12 per share and \$1.00 per share in 2006, 2005 and 2004, respectively. The 2006 dividend represented a 10 percent increase from 2005, and the 2005 dividend represented a 12 percent increase from 2004.

### *Off-Balance Sheet Arrangements and Aggregate Contractual Obligations*

#### *Off-Balance Sheet Arrangements*

In accordance with the definition under SEC rules, the following qualify as off-balance sheet arrangements:

- any obligation under certain guarantee contracts;
- a retained or contingent interest in assets transferred to an unconsolidated entity or similar arrangement that serves as credit, liquidity or market risk support to that entity for such assets;
- any obligation under certain derivative instruments; and
- any obligation arising out of a material variable interest held by the registrant in an unconsolidated entity that provides financing, liquidity, market risk or credit risk support to the registrant, or engages in leasing, hedging or research and development services with the registrant.

As of December 31, 2006, our Company was contingently liable for guarantees of indebtedness owed by third parties in the amount of approximately \$270 million. Management concluded that the likelihood of any material amounts being paid by our Company under these guarantees is not probable. As of December 31, 2006, we were not directly liable for the debt of any unconsolidated entity, and we did not have any retained or contingent interest in assets as defined above.

Our Company recognizes all derivatives as either assets or liabilities at fair value in our consolidated balance sheets. Refer to Note 12 of Notes to Consolidated Financial Statements.

In December 2003, we granted a \$250 million standby line of credit to Coca-Cola FEMSA with normal market terms. This standby line of credit expired in December 2006.

### Aggregate Contractual Obligations

As of December 31, 2006, the Company's contractual obligations, including payments due by period, were as follows (in millions):

	Payments Due by Period				
	Total	2007	2008-2009	2010-2011	2012 and Thereafter
Short-term loans and notes payable <sup>1</sup> :					
Commercial paper borrowings	\$ 1,942	\$ 1,942	\$ —	\$ —	\$ —
Lines of credit and other short-term borrowings	225	225	—	—	—
Liability to CCEAG shareowners <sup>2</sup>	1,068	1,068	—	—	—
Current maturities of long-term debt <sup>3</sup>	33	33	—	—	—
Long-term debt, net of current maturities <sup>3</sup>	1,314	—	611	576	127
Estimated interest payments <sup>4</sup>	993	80	135	73	705
Purchase obligations <sup>5</sup>	8,401	4,815	1,237	636	1,713
Marketing obligations <sup>6</sup>	3,925	1,579	832	583	931
Lease obligations	545	141	193	127	84
<b>Total contractual obligations</b>	<b>\$ 18,446</b>	<b>\$ 9,883</b>	<b>\$ 3,008</b>	<b>\$ 1,995</b>	<b>\$ 3,560</b>

<sup>1</sup> Refer to Note 8 of Notes to Consolidated Financial Statements for information regarding short-term loans and notes payable. Upon payment of outstanding commercial paper, we typically issue new commercial paper. Lines of credit and other short-term borrowings are expected to fluctuate depending upon current liquidity needs, especially at international subsidiaries.

<sup>2</sup> Refer to Note 8 of Notes to Consolidated Financial Statements for a discussion of our liability to CCEAG shareowners as of December 31, 2006. We paid the amount due to CCEAG shareowners in January 2007 to discharge our liability.

<sup>3</sup> Refer to Note 9 of Notes to Consolidated Financial Statements for information regarding long-term debt. We will consider several alternatives to settle this long-term debt, including the use of cash flows from operating activities, issuance of commercial paper or issuance of other long-term debt.

<sup>4</sup> We calculated estimated interest payments for long-term debt as follows: for fixed-rate debt and term debt, we calculated interest based on the applicable rates and payment dates; for variable-rate debt and/or non-term debt, we estimated interest rates and payment dates based on our determination of the most likely scenarios for each relevant debt instrument. We typically expect to settle such interest payments with cash flows from operating activities and/or short-term borrowings.

<sup>5</sup> The purchase obligations include agreements to purchase goods or services that are enforceable and legally binding and that specify all significant terms, including long-term contractual obligations, open purchase orders, accounts payable and certain accrued liabilities. We expect to fund these obligations with cash flows from operating activities.

<sup>6</sup> We expect to fund these marketing obligations with cash flows from operating activities.

In accordance with SFAS No. 87, "Employers' Accounting for Pensions," and SFAS No. 106, "Employers' Accounting for Postretirement Benefits Other Than Pensions," as amended by SFAS No. 158, "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans—an amendment of FASB Statements No. 87, 88, 106, and 132(R)," the total accrued benefit liability for pension and other postretirement benefit plans recognized as of December 31, 2006, was \$1,273 million. Refer to Note 16 of Notes to Consolidated Financial Statements. This accrued liability is included in the consolidated balance sheet line item other liabilities. This amount is impacted by, among other items, pension expense funding levels, changes in plan demographics and assumptions, investment return on plan assets, and the application of SFAS No. 158. Because the accrued liability does not represent expected liquidity needs, we did not include this amount in the contractual obligations table.

The Pension Protection Act of 2006 (“PPA”) was enacted in August 2006 and established, among other things, new standards for funding of U.S. defined benefit pension plans. One of the primary objectives of the PPA is to improve the financial integrity of underfunded plans through the requirement of additional contributions. The requirements of the PPA will not have a significant impact on our financial condition because, under the provisions of the PPA, the minimum required contribution for the primary funded U.S. plan is projected to be zero through 2017 as a result of contributions we have made to the plan since 2001. Therefore, we did not include any amounts as a contractual obligation in the above table. We may, however, decide to make additional discretionary contributions to our pension and other benefit plans in future years. In addition, as a result of contributions totaling approximately \$224 million in 2006 to fund a portion of our U.S. postretirement healthcare obligation, including a contribution of \$216 million to a VEBA trust, we do not expect to contribute to our U.S. postretirement healthcare plan in 2007. We generally expect to fund all future contributions with cash flows from operating activities.

Our international pension plans are funded in accordance with local laws and income tax regulations. We do not expect contributions to these plans to be material in 2007 or thereafter. Therefore, no amounts have been included in the table above.

As of December 31, 2006, the projected benefit obligation of the U.S. qualified pension plans was \$1,660 million, and the fair value of plan assets was \$2,120 million. As of December 31, 2006, the projected benefit obligation of all pension plans other than the U.S. qualified pension plans was \$1,385 million, and the fair value of all other pension plan assets was \$723 million. The majority of this underfunding is attributable to an international pension plan for certain non-U.S. employees that is unfunded due to tax law restrictions, as well as our unfunded U.S. nonqualified pension plans. These U.S. nonqualified pension plans provide, for certain associates, benefits that are not permitted to be funded through a qualified plan because of limits imposed by the Internal Revenue Code of 1986. Disclosure of amounts are not included in the above table regarding expected benefit payments for our unfunded pension plans. However, we anticipate annual benefit payments to be in the range of approximately \$25 million to \$30 million in 2007 and to remain at or near this annual level for the next several years. We can not reasonably estimate these payments for 2012 and thereafter due to the ongoing nature of the obligations under these plans.

Deferred income tax liabilities as of December 31, 2006, were \$641 million. Refer to Note 17 of Notes to Consolidated Financial Statements. This amount is not included in the total contractual obligations table because we believe this presentation would not be meaningful. Deferred income tax liabilities are calculated based on temporary differences between the tax bases of assets and liabilities and their respective book bases, which will result in taxable amounts in future years when the liabilities are settled at their reported financial statement amounts. The results of these calculations do not have a direct connection with the amount of cash taxes to be paid in any future periods. As a result, scheduling deferred income tax liabilities as payments due by period could be misleading, because this scheduling would not relate to liquidity needs.

Minority interests of \$358 million as of December 31, 2006, for consolidated entities in which we do not have a 100 percent ownership interest were recorded in the consolidated balance sheet line item other liabilities. Such minority interests are not liabilities requiring the use of cash or other resources; therefore, this amount is excluded from the contractual obligations table.

### *Foreign Exchange*

Our international operations are subject to opportunities and risks relating to foreign currency fluctuations and governmental actions. We closely monitor our operations in each country and seek to adopt appropriate strategies that are responsive to fluctuations in foreign currency exchange rates.

We use 64 functional currencies. Due to our global operations, weaknesses in some of these currencies might be offset by strength in others. In 2006, 2005 and 2004, the weighted-average exchange rates for foreign

currencies in which the Company conducted operations (all operating currencies), and for certain individual currencies, strengthened (weakened) against the U.S. dollar as follows:

Year Ended December 31,	2006	2005	2004
All operating currencies	(1)%	2 %	6 %
Brazilian real	10 %	21 %	5 %
Mexican peso	0 %	4 %	(5)%
Australian dollar	(1)%	3 %	13 %
South African rand	(7)%	1 %	18 %
British pound	1 %	0 %	12 %
Euro	1 %	1 %	9 %
Japanese yen	(6)%	(1)%	7 %

These percentages do not include the effects of our hedging activities and, therefore, do not reflect the actual impact of fluctuations in exchange rates on our operating results. Our foreign currency management program is designed to mitigate, over time, a portion of the impact of exchange rate changes on our net income and earnings per share. The total currency impact on operating income, including the effect of our hedging activities, was a decrease of approximately 1 percent in 2006. The impact of a weaker U.S. dollar increased our operating income by approximately 4 percent and 8 percent in 2005 and 2004, respectively. The Company currently expects currencies to have little impact on operating income in 2007.

Exchange losses—net amounted to approximately \$15 million in 2006, \$23 million in 2005 and \$39 million in 2004 and were recorded in other income (loss)—net in our consolidated statements of income. Exchange losses—net include the remeasurement of monetary assets and liabilities from certain currencies into functional currencies and the costs of hedging certain exposures of our consolidated balance sheets. Refer to Note 12 of Notes to Consolidated Financial Statements.

The Company will continue to manage its foreign currency exposure to mitigate, over time, a portion of the impact of exchange rate changes on net income and earnings per share.

### ***Overview of Financial Position***

Our consolidated balance sheet as of December 31, 2006, compared to our consolidated balance sheet as of December 31, 2005, was impacted by the following:

- increases in trademarks with indefinite lives, goodwill and other intangible assets of \$99 million, \$356 million and \$859 million, respectively, primarily due to our acquisitions of CCCIL, Apollinaris and TJC as well as the consolidation of Brucephil in 2006;
- an increase in property, plant and equipment of \$1,727 million, primarily due to 2006 purchases and acquisitions and consolidation under Interpretation No. 46(R), as discussed above; and
- a decrease in loans and notes payable of \$1,283 million, primarily due to the net repayment of commercial paper and short-term debt during 2006.

### ***Impact of Inflation and Changing Prices***

Inflation affects the way we operate in many markets around the world. In general, we believe that, over time, we are able to increase prices to counteract the majority of the inflationary effects of increasing costs and to generate sufficient cash flows to maintain our productive capability.

**Additional Information**

Effective January 1, 2007, we combined the Eurasia and Middle East Division, and the Russia, Ukraine and Belarus Division, both of which were previously included in the North Asia, Eurasia and Middle East operating segment, with the India Division, previously included in the East, South Asia and Pacific Rim operating segment, to form the Eurasia operating segment; and we combined the China Division and the Japan Division, previously included in the North Asia, Eurasia and Middle East operating segment, with the remaining East, South Asia and Pacific Rim operating segment to form the Pacific operating segment. As a result, beginning with the first quarter of 2007, our organizational structure will consist of the following operating segments: Africa; Eurasia; European Union; Latin America; North America; Pacific; Bottling Investments; and Corporate.

For information concerning our operating segments as of December 31, 2006, refer to Note 20 of Notes to Consolidated Financial Statements.