

Creating Powerful CEO Communications

Connecting Culture and Leadership



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Connecting Culture and Leadership

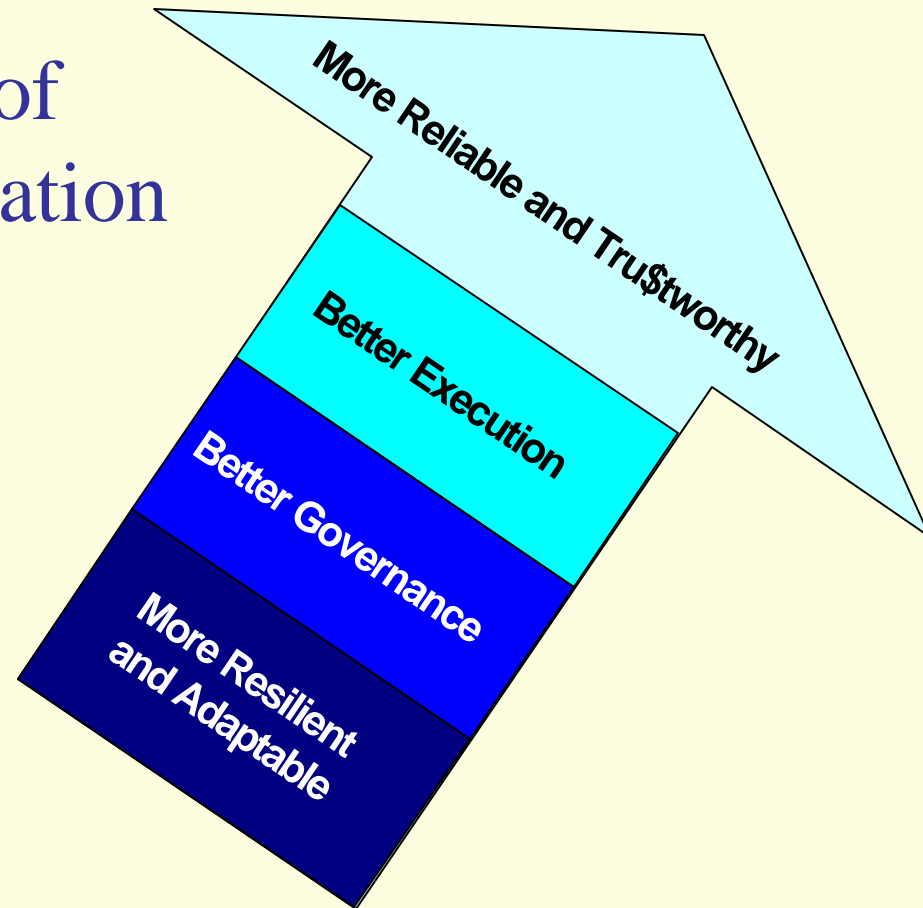
How Can CEO Letters Build Tru\$t?

1. Gauges accounting integrity – values determine numbers
2. Signed by CEO – personal accountability
3. Not regulated – creative, trust-building opportunity
4. Reveals depth of understanding about the business
5. Continuity of Vision – some investors keep five years of annuals to check on continuity

CEO letters demonstrate the strength or weakness of a CEO's communication advantage.

Connecting Culture and Leadership

The Benefits of CEO Communication Advantage



To find reliable, trustworthy businesses,
look for the alignment of leadership and culture.

Connecting Culture and Leadership

Our CEO Letter Research Reveals Four Kinds of Companies

Strong Alignment of Culture and Leadership

Berkshire Hathaway

Continental Airlines

PepsiCo

Wells Fargo

Weak Alignment of Culture and Leadership

3M

Boeing

Coca-Cola

Westinghouse

Alignment Anomaly

Home Depot

Pfizer

Expected strong alignment, is not supported by the model.

Indeterminate Alignment

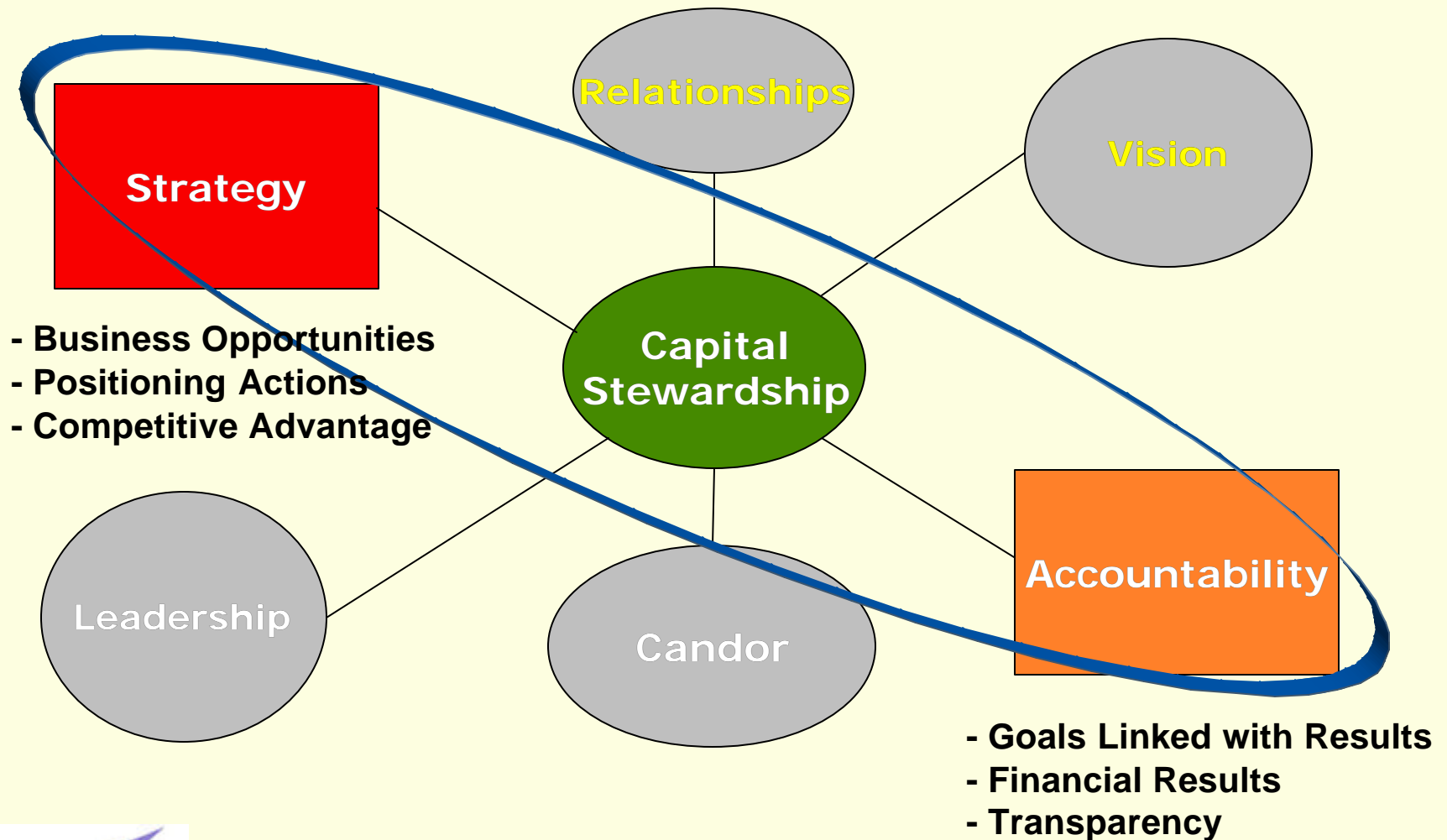
MBNA

Trump Hotels

Insufficient information to evaluate alignment.

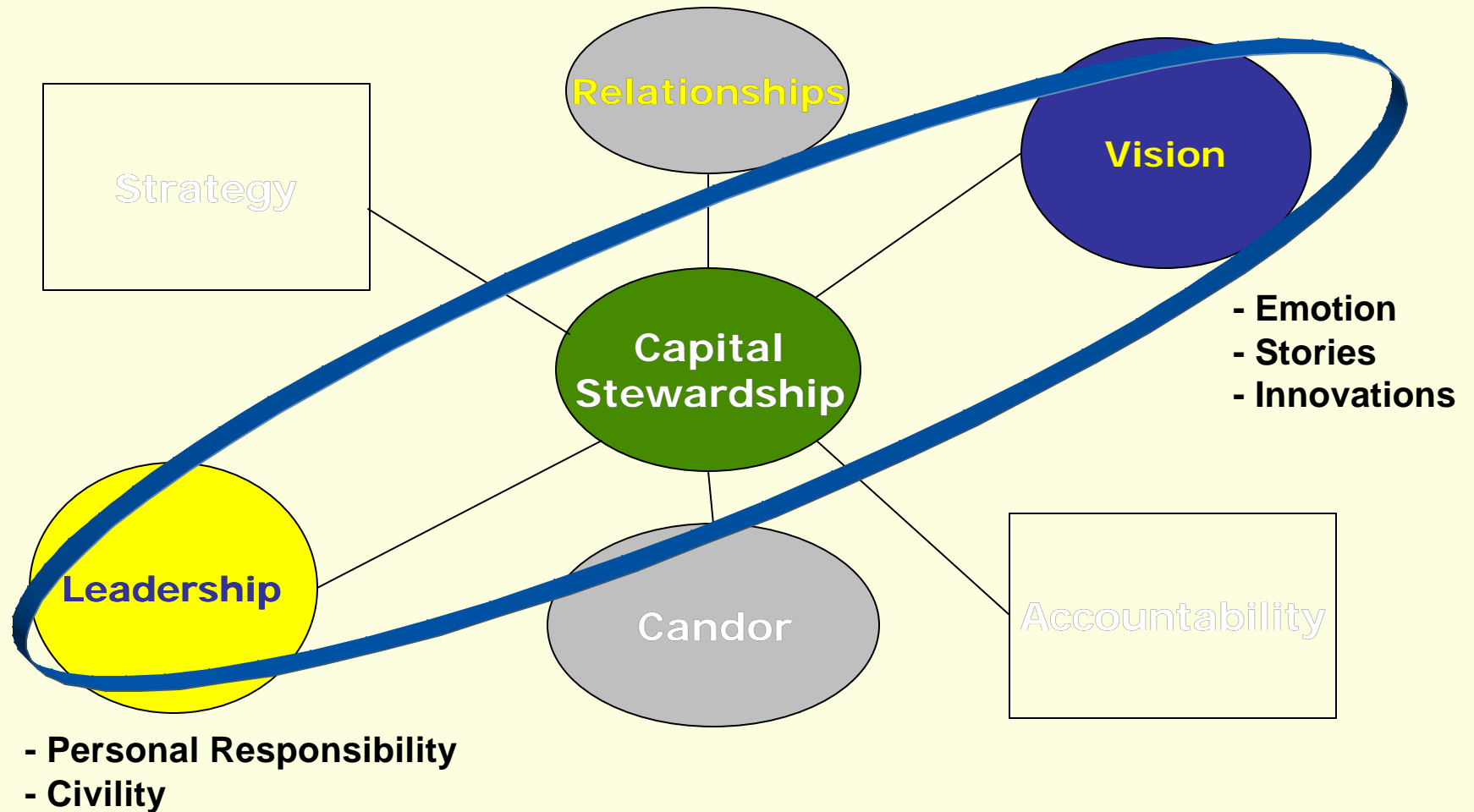
The Rittenhouse Model™ of The Anatomy of a Business

Left Brain Subsystem



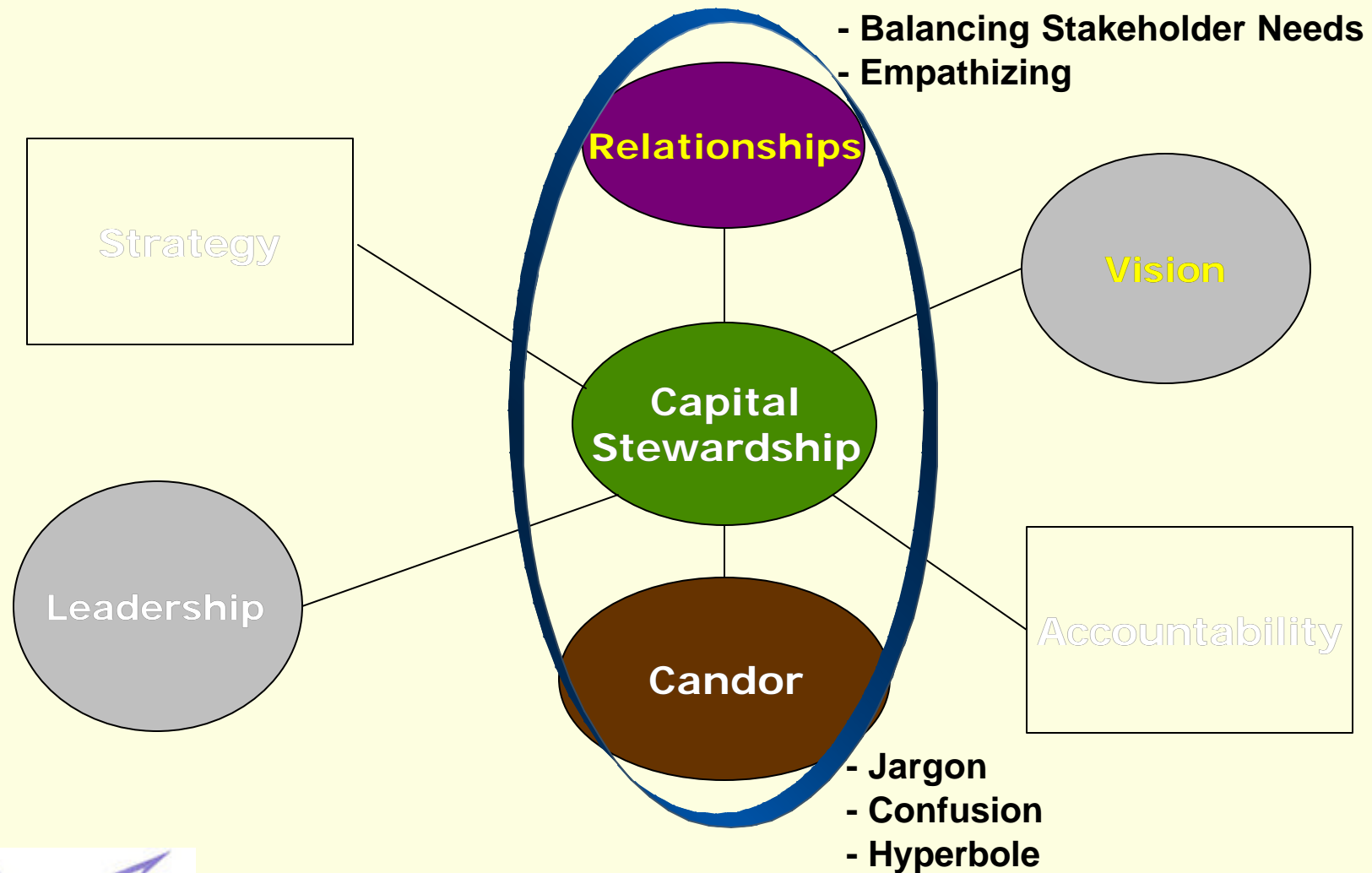
The Rittenhouse Model™ of the Anatomy of a Business

Right Brain Subsystem

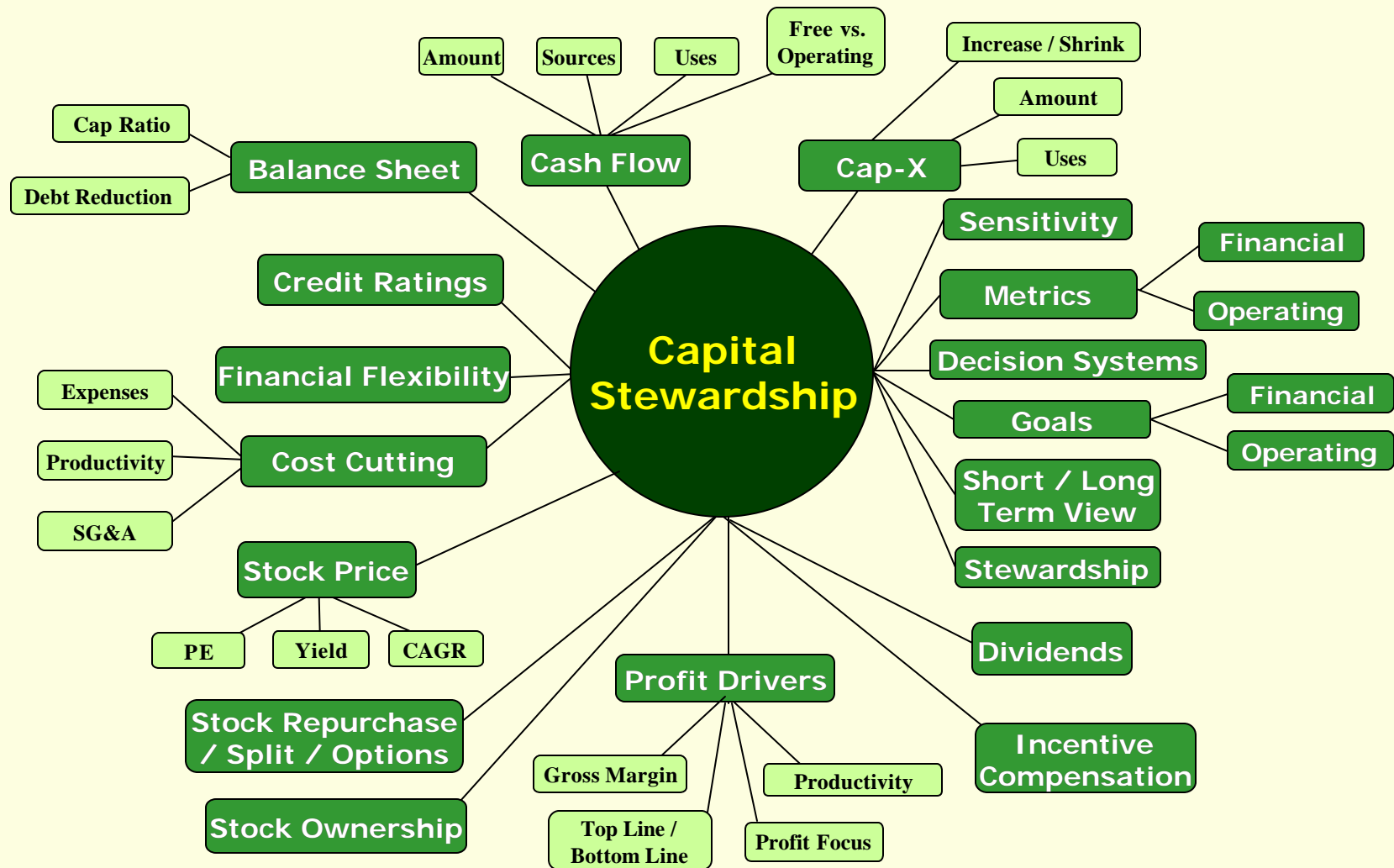


The Rittenhouse Model™ of the Anatomy of a Business

Backbone Subsystem




Businesses that build investor trust and achieve sustained superior results put Capital Stewardship in the center.



GE reports on 20 out of 21 Capital Stewardship topics in the 2002 CEO letter.

Investors equate strong corporate governance with capital stewardship practices and attitudes. GE excels in communicating the importance of capital stewardship.

Company	(1) Cash Flow	(2) Financial Goals	(3) Operating Goals	(4) Profit Drivers	(5) Financial Metrics	(6) Operating Metrics	(7) Sensitivity	(8) Decision Criteria	(9) Cap-Ex	(10) Credit Rating
GE	45	41		38	15	15	5	15	36	6



(11) Bal. Sheet / Cap Ratio	(12) Financial Flexibility	(13) Cost Cutting	(14) Expense / Pro-ductivity	(15) Incentive Comp.	(16) Insider Ownership	(17) Steward-ship	(18) Short / Long-Term	(19) Stock Price	(20) Stock Split/ Repurchase	(21) Divi- dend	Total
6	6	12	9	18	15	6	16	6	6	12	328

Capital Stewardship

Examples of Detailed Cash Flow Reporting in GE 2002 Letter

Sustainable cash

- ✍ I believe that our reputation for integrity and honorable dealings is our most important asset. GE has not been immune to the fallout from recent bull and bubble markets. I hear from investors who are concerned about the quality of corporate earnings, the need for a solid balance sheet and sustainable cash flow, and the importance of responsible executive compensation and accounting standards. Let me assure you that GE will lead on all of these fronts.

Cash – results

- ✍ GE is strong. In 2002, we grew earnings 7% and cash 10% in a tough economy, and our businesses improved their global positions with investments in technology and customer focus. We maintained our financial strength, remaining one of only seven Triple A-rated industrial companies, and GE's terrific people prepared your company for success in the 21st century. There is much to be proud of.
- ✍ Cash flow from operating activities (excluding progress collections) reached \$15.2 billion, up 10%. Operating margin and return on average total capital remained near historic highs at 19% and 24%, respectively.

Customer cash

- ✍ Strong processes are the foundation of our operating rigor. We are in the ninth year of Six Sigma at GE, and it has become a permanent initiative — Six Sigma is the way we work. During the last year we completed more than 50,000 projects, focused primarily in three areas: working with our customers on their issues; improving our internal processes to improve our customer interfaces and generate cash; and improving the flow of high-technology products and services to the marketplace.

Capital Stewardship (cont'd)

Example of Detailed Cash Flow Reporting in GE 2002 Letter

Cash as goal

- Increasingly, the focus of our operating rigor is on growing cash flow. Cash is a priority for our leadership team and represents 60% of the measurement used for their incentive compensation. Six Sigma is creating repeatable and reliable processes that allow us to reduce cash tied up in inventory and receivables. Through digitization we are getting more from our fixed assets. We plan to generate nearly \$30 billion in operating cash flow ex-progress in 2002-2003.

Liquidity

- We took several actions to strengthen our balance sheet in 2002. We improved our liquidity by reducing the commercial paper of our financial services businesses to 31% of their total debt outstanding. We also infused more than \$6 billion into those businesses to increase capital and reduce leverage. GE's Triple A rating was affirmed by the rating agencies, and our rigorous approach was recognized. We received our awards, including "Borrower of the Year" and "Best Corporate Issuer," from bond investors and underwriters surveyed by *International Finance Review*.

Cash strategy

- Acquisitions are a key form of investment for us. We have invested nearly \$35 billion in acquisitions over the past two years. Acquisitions are a way to redeploy cash flow for future growth. The key is discipline: we buy the right businesses at the right price and grow them. Our acquisitions tend to be between \$100 million and \$2 billion in value, in industries we know. Our industrial acquisitions are companies with high margin rates and low capital requirements where GE can boost growth and cash flow. Our financial services businesses consolidate portfolios when GE can improve funding cost, risk management and growth. Our investment screen is simple: we expect a 15% cash-on-cash return by year five, or we don't do the deal.

Other Examples of “Cash” Reporting and Efficient Communication

Sherwin Williams 2001 Shareholder Letter

In a year of lower sales and earnings, investors look for signs of strength, such as a company’s ability to generate cash. (3)
This past year, through excellent management of working capital, (3) we increased free cash flow by \$145.65 million (3) to a record \$388.09 million. (3) We define free cash flow as net operating cash available after dividend payments and capital expenditures. (3) (15 points)

This best-in-class example is detailed and comprehensive.

- ✍ Reports cash flow dollars.
- ✍ Defines free cash flow.
- ✍ Describes uses of cash flow.
- ✍ Identifies source of cash flow increase – better working capital management.

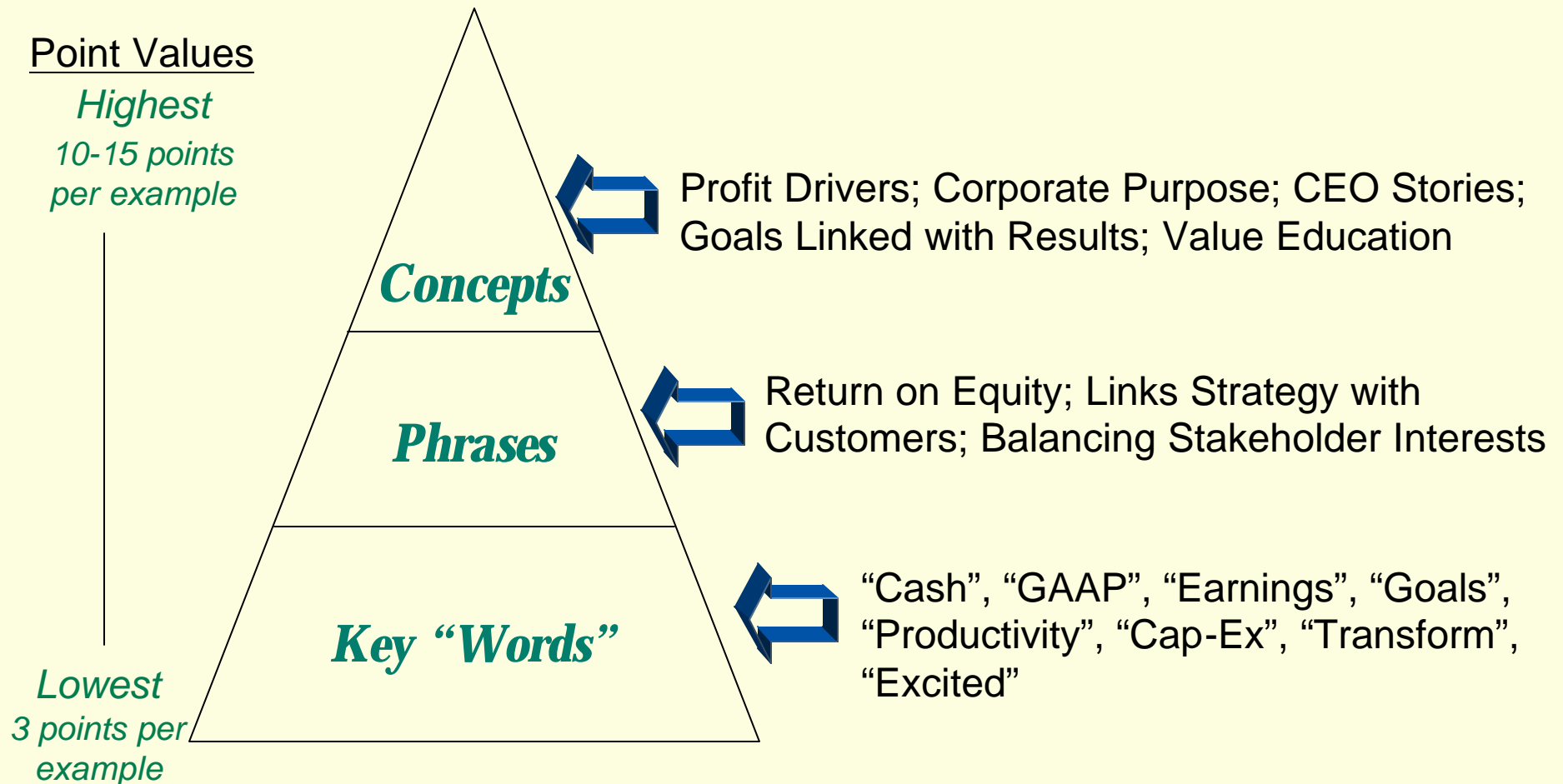
General Motors 2001 Shareholder Letter

As we move into 2002, we are aggressively pursuing additional structural and material cost reductions, and intensifying our focus on cash generation. (3 points)

Cursory Description

Sherwin Williams is more efficient because they provide five times more meaning than does General Motors and use only 2.2 times the lineage.

How to Quantify CEO Language: Analyze Words, Phrases and Concepts



Example of Concepts: Profit Drivers

PepsiCo 2002 Shareholder Letter

Profit opportunity

With the broad appeal of our brands, almost every market on earth represents potential growth. Yet today only about 30% of our revenues and 20% of operating profits come from outside the United States and Canada. That's a world of opportunity.

Profitable growth goal

Rules and policies are important. But they can't substitute for individual integrity. We believe that the sound governance of PepsiCo rests on hiring and retaining the right people and creating the right atmosphere. We certainly need people who are smart and competent, but above that our people must be ethical. And on the assumption that even good people make honest mistakes, we must foster an environment of checks and balances — where all actions are transparent and open to challenge. Promoting a workplace where honest people feel free to challenge ideas and practices is one of the best ways we know to achieve our goal of strong, sustainable, profitable growth while preserving the highest ethical standards.

Our brands drive more sales growth, profit growth and cash flow for big U.S. retailers than those of any other food or beverage manufacturer.

Put it all together and one thing is very clear: PepsiCo is strong and healthy and well equipped to succeed. We have a portfolio of great businesses that generate real sales and real profits. We have strong market positions and genuine competitive advantages. Best of all, we have more than 140,000 outstanding people who are dedicated to serving the interests of shareholders — with passion, commitment and integrity.

Division operating profit grew 11%.



Example of Concepts: Profit Drivers (Cont'd)

PepsiCo 2002 Shareholder Letter

Profitable distribution system

Consumption of our brands is highly elastic. If we make it easy for people to buy more of our products, often they do. So we work to make our brands available everywhere someone might want them. But we have to do it profitably. A distribution system that's cost-efficient for one product may not work for another.

PepsiCo has another big advantage. Today we have not one, but several large-scale distribution systems, enabling us to cost-effectively distribute a wide range of products:

Direct-store-delivery (DSD) systems at Frito-Lay and through Pepsi-Cola bottlers are ideal for products that move through stores quickly, require delicate handling or benefit from careful merchandising. These systems reach more than 2 million retail customers each week, from the largest club stores to the smallest "mom-and-pop" outlets.

A large broker-warehouse distribution system moves Quaker, Gatorade and Tropicana products to large retail outlets at a low cost — and allows us to test new products that are too small for economic distribution via DSD.

A national distribution system focused on foodservice and vending accounts — one of the largest of its kind — gives Frito-Lay, Quaker, Gatorade and Tropicana access to a growing channel that few competitors can serve efficiently.

A small but growing "chilled" DSD system distributes products requiring refrigeration. Created for Tropicana juices, it could carry many other products as well.

Hybrid systems, using elements of our various distribution systems, enable us to reach large numbers of retailers in emerging markets like India and China.



Summary Analysis of Communication Stewardship

Coca-Cola & PepsiCo

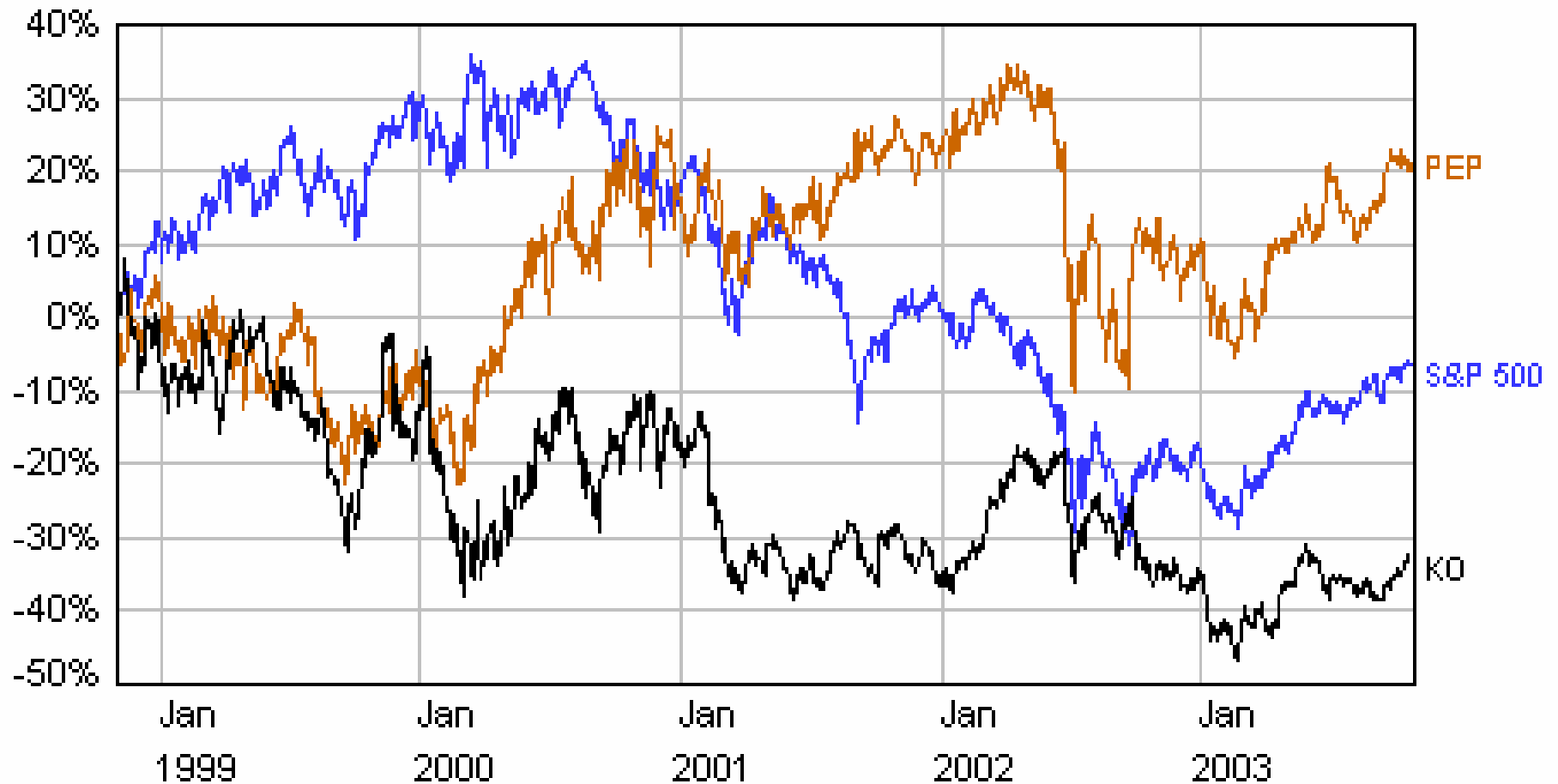
Shareholder Letter Scoring

Content Scores

Company	Gross Score	Corporate Fog	Net Content Total
Coca-Cola 2002	415	-224	191
Coca-Cola 1999	259	-128	131
Coca-Cola 1996	831	-90	741
PepsiCo 2002	815	-57	758
PepsiCo 1996	841	-56	785

Stock Price Performance Coca-Cola and PepsiCo

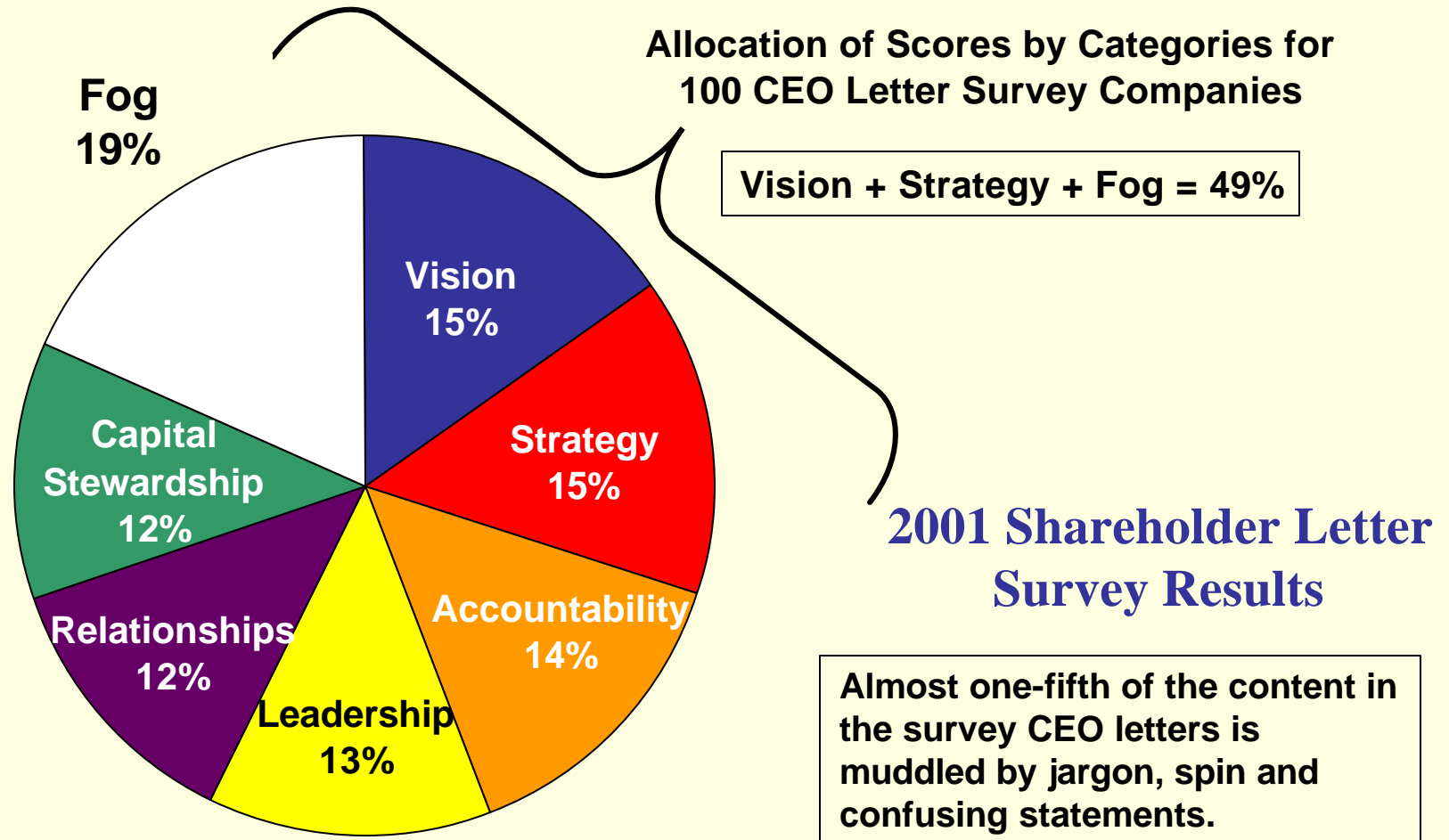
11/11/1998 – 11/11/2003



Data provided by S&P Comstock

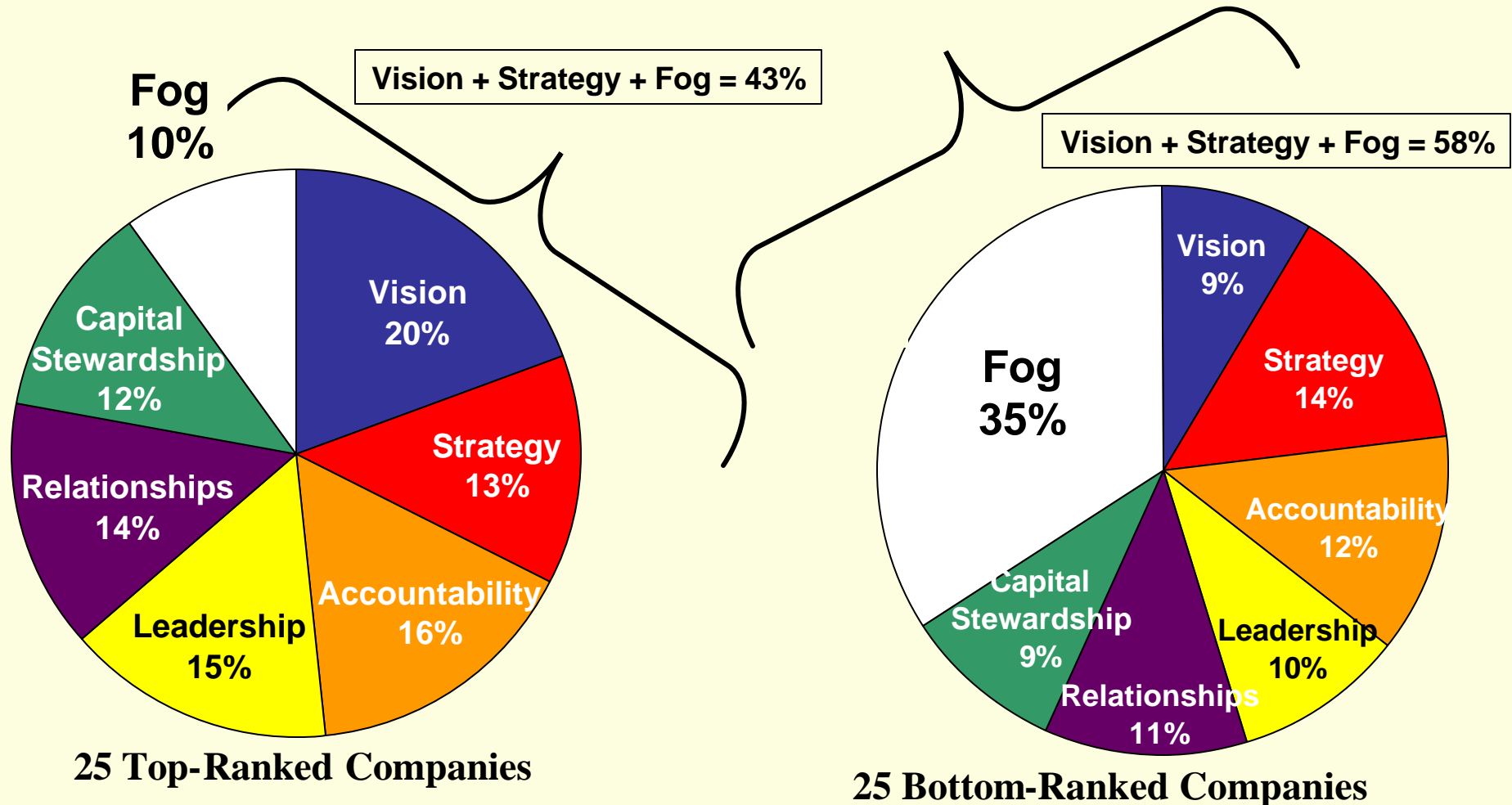
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Balancing Business Systems Determines Success



100 Companies from 15 Different Industries

Balancing Business Systems Determines Success



Vision and Fog account for the greatest differences in scores between top and bottom-ranked 2001 CEO Letter Survey companies.

Connecting Culture and Leadership

Balancing Business Systems Determines Success



PepsiCo
2002 Shareholder Letter



Coca-Cola
2002 Shareholder Letter

Examples of Fog

Coca-Cola 2002 Shareholder Letter

Jargon

✍ To better realize opportunities for growth in 2002, I focused the Company on: 1) profitable diversification and expansion of our range of products while advancing our core brands; 2) improving working relationships with our bottling partners around the world; 3) building an integrated team operating with heightened focus on corporate governance and financial transparency.

Confusion, Jargon and Spin

Fails to mention that 2001 EPS was \$1.60; how is this transparent?

The Coca-Cola Company in 2002 achieved worldwide unit case volume growth of 5 percent, nearly 950 million incremental unit cases. Excluding volume associated with the brands acquired during 2002, our growth rate was 4.5 percent. Cash from operations was a record \$4.7 billion, a 15 percent increase over 2001. After investing activities, we generated \$3.6 billion of cash flow in 2002, a 22 percent increase. Reported earnings per share were \$1.23 after a reduction of \$0.54 resulting from accounting changes and several other items, including \$0.11 per share impact from stock option expense. Throughout the year, we outpaced the rest of the industry in each of the major beverage categories in nearly every key global market.

Stock Price Change Analysis Summary Results

2001-1999 Shareholder Letter Surveys

2001	<u>Top 25 Companies</u>	<u>Bottom 25 Companies</u>	<u>↓</u>	<u>S&P 500</u>
1 Year	1.2%	-8.0%	+9.2%	-10.5%
2 Years	-12.7%	-19.9%	+7.2%	-31.4%
<hr/>				
2000				
1 Year	16.5%	-3.8%	+20.3%	-10.1%
2 Years	4.7%	-8.8%	+13.5%	-21.9%
<hr/>				
1999				
1 Year	22.8%	-2.6%	+25.4%	19.5%
2 Years	9.0%	18.0%	-9.0% ⁽¹⁾	7.4%
<hr/>				
1.75 Years	12.8%	-0.7%	+13.5%	4.3%
2.25 Years	2.7%	5.9%	-3.2%	-5.6%

⁽¹⁾ End of this period coincides with results of 2000 Election and deflation of the techno-bubble.

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The Do's and Don'ts of Shareholder Letter Writing

Do's

1. Address key issues and questions that would rather be ignored.
2. Conform letter content and tone with Financial Statements and MD&A.
3. Integrate stakeholder perspectives.

Don'ts

1. Pretend that you are starting from scratch – look back.
2. Limit letter reviews to insiders.
3. Lose the opportunity to capitalize on the marketing and governance power of the letter.

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